

ALAGAPPA UNIVERSITY

(Accredited with 'A' Grade by NAAC)
Karaikudi 630 003



DIRECTORATE OF DISTANCE EDUCATION

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82

M.B.A. (Corporate Secretaryship)



Paper - ~~4.3~~ 4.5

Secretarial and Management Audit

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PAPER - 4.3

Secretarial and Management Audit

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PAPER SECRETARIAL AND MANAGEMENT AUDIT

UNIT I

Company Secretary in Practice: Various recognitions and areas of practice – Advisory services rendered – Challenges before the profession – Professional standards and code of conduct – Exploring new horizons.

UNIT II

Secretarial Audit: Need, objectives and scope – Periodicity and format for secretarial audit report – Appointment, duties and powers of secretarial auditor – Check-list/ Worksheet for secretarial audit under various corporate laws and covenants of loan agreements entered into with financial institutions.

UNIT III

Search / Status Reports: Preparation of search and status reports from Registrar of Companies records for banks and financial institutions – Scope and importance – Verification of documents relating to charges – Requirements of various financial institutions and other corporate lenders.

UNIT IV

Securities Audit: Meaning, need and scope – Ensuring proper compliance of provisions relating to issue and transfer of securities – Preventing fraudulent and unfair trade practices including securities and Exchange Board of India regulations framed thereon – Protecting the interest of investors.

UNIT V

Compliance Certificate: Concept and need – Appraisal of secretarial compliances – Specimen compliance certificate.

UNIT VI

Management Audit: Meaning, nature and scope – Principles and fundamentals of management audit – Appraisal of management methods of performance – Organisational needs for management audit.

UNIT VII

Cost Audit: Nature, objectives and scope – Cost audit distinguished from financial audit and management audit – Cost audit as an aid to management, shareholders and other external agencies and public – Cost audit report.

UNIT VIII

Registers and Returns: Statutory and non-statutory registers to be maintained under the Companies Act – Returns to be filed with Register of Companies.

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1. Shanbhogue K V, *Filing of Forms and Returns and Application under Company Law*, Law Publishing House, Allahabad.
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LESSON – 1

COMPANY SECRETARY IN PRACTICE

Objective:

After reading this lesson, the students should be able to under stand the significance of Company Secretary in Practice, recognitions secured for the practising company secretaries and the various areas of practice:

Learning Activities:

Reading of

i. Secretarial, Securities and Management audit
by Dr.V.Balachandran & K.S.Ravichandran
Bharath Law Book House, New Delhi

ii. Master Guide for Company Secretaries
by S.Kannan, Taxmann Publishers, New Delhi

iii. ICSI Study Materials

Contents:

- Introduction:
- Areas of Practice:
- Company Secretary in Practice:
- Who can Practise as Company Secretary?
- Certificate of Practice:
- Clarification regarding use of Designation by members in Practice:
- Renewal of Certificate of Practice (Reg.10)
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- Certification by Practising Company Secretary:
- Recognitions for Company Secretaries in Practice under the Companies Act and Regulations:
- Other Services:
- Professional Misconduct:
- Contents of the First and Second Schedules to the Act:

Introduction:

Section 2(2) of the Company Secretaries Act, 1980 indicates the various areas of practice issued by institute. The objective of authorizing qualified members to practice is to make available professional services of a company secretary to the corporate sector, including small and medium sized companies which are not required by law, to employ compulsorily a whole-time qualified company secretary.

The concept of Company Secretary in practice has taken firm roots with the recognition of company secretary in practice under section 2(45A) of Companies Act, 1956. Besides the statutory recognition, a company secretary in practice has been conferred recognition under section 22(2), 149, 161 and Schedule XIII of the Companies Act, 1956. In addition some state financial institutions including the Manipur Industrial Development Corporation Ltd., Assam Industrial Development Corporation Ltd., Gujarat Industrial Development Corporation Ltd. and Financial Corporation Ltd. have already introduce the concept of Secretarial Audit in respect of Companies assisted by them. These corporations have prescribed annual Secretarial Audit of Companies for the assisted companies to be conducted in the manner prescribed by the Institute. A number of other financial / investment / industrial development corporations are also considering to introduce Secretarial Audit in companies assisted by them in view of the inherent benefits of such an audit.

The Department's circulars Nos.14/90 dated 5.9.90 and 5/91 dated 26.2.91 directing Registers or Companies to taken on record all documents filed by companies within a reasonable period of say ten days if the same are certified by a Company Secretary in Practice, with a view to avoid delay in registration of documents, is another significant development for the practicing side of the profession.

Areas of Practice:

Section 2(2) of the Company Secretaries Act, 1980 (hereinafter called the Act) provides that a member of the Institute shall be deemed to be in practice when, individually or in partnership with one or more members of the Institute in practice or in partnership with members of such other recognized professions as

may be prescribed, does any of the following in consideration of remuneration received or to be received:

(a) engages himself in the practice of the profession of company secretaries to, or in relation to, any company; or

(b) offers to perform or performs services in relation to the promotion, formation, incorporation, amalgamation, reconstruction, reorganisation or winding up of companies; or

(c) offers to perform or performs such services as may be performed by

(i) an authorised representative of a company with respect to filing, registering, presenting, attesting or verifying any documents (including forms, applications and returns) by or on behalf of the company,

(ii) a share transfer agent,

(iii) an issue house,

(iv) a share and stock broker,

(v) a secretarial auditor or consultant,

(vi) an advisor to the company on management including any legal or procedural matter falling under the Capital Issues (Control) Act, 1947, the Industries (Development and Regulation) Act, 1951, the Companies Act, 1956, any of the rules or bye-laws made by a recognized stock exchange, the Monopolies and Restrictive Trade Practices Act, 1969, the Foreign exchange Regulation Act, 1973, or under any other law for the time being in force;

(vii) issuing certificates on behalf of or for the purposes of, a company.

(d) holds himself out to the public as a company secretary in practice; or

(e) renters professional services or assistance with respect to matters of principle or detail relating to the practice of the profession of company secretaries; or

(f) renders such other services, as in the opinion of the Council are or may be rendered by a company secretary in practice.

Company Secretary in Practice:

A company secretary may be said to be in practice when, instead o accepting employment as secretary of a company, he chooses to practice independently as a company secretary, either individually or in partnership with one or more practicing company secretaries.

According to section 2(2) of the Company Secretaries Act, 1980, save as otherwise provided in this Act, a member of the Institute of Company Secretaries of India shall be deemed "to be in practice" when, individually or in partnership with one or more members of the Institute in practice or in partnership with members of such other recognized professions as may be prescribed, he, in consideration of remuneration received or to be received, engages /offers himself in the various activities specified in this section.

Who can Practice as Company Secretary?

Section 6 of the Company Secretaries Act, 1980 provides that no member of the Institute shall be entitled to practice, whether in India or elsewhere, unless he has obtained from the Council a Certificate of Practice.

A member who desires to be entitled to practice should make an application in the prescribed form and pay such annual fee for his certificate as may be prescribed. Such fee shall be payable on or before the 1st day of April in each year. At present the annual fee for Certificate of Practice is Rs.75 (vide Schedule B of the Regulations).

Certificate of Practice:

Regulation 10 of the Company Secretaries Regulations, 1982 provides that a member of the Institute may apply in appropriate form for the issue of a Certificate of Practice entitling him to practice as Company Secretary anywhere in India [Reg.10(1)]. On acceptance of the application, the council of the Institute shall issue the certificate in appropriate form which shall be valid until cancelled [Reg.10(2)]. In the case of renewal of the certificate of practice, the secretary to the Council shall issue a letter extending the validity of the certificate for that year in appropriate form. [Reg.(10(3))]. If the member ceases to be in practice, he must forthwith intimate the fact to the Secretary within not

later than 30 days from the date when he ceases to be in practice [Reg. 10(4)]. A member who ceases to be in practice or whose certificate of practice has been cancelled under Regulation 11, must forthwith surrender the certificate to the secretary to the Council [Reg.10(5)].

Clarification regarding use of Designation by members in Practice:

Under section 7 of the Company Secretaries Act, 1980, every member of the Institute of Company Secretary and shall not use any other designation, whether in addition thereto or in substitution thereof. The use of designations "Practicing Company Secretary", "Company Secretary in Practice" or "Company Secretary in Whole-time Practice" was earlier held to be 'not permitted' under section 7 of the Act for use by members in practice. Therefore, the members in practice were bound to use the designation "Company Secretary" only.

The council of the ICSI has recently reconsidered its earlier view, (CS / NOV 2000 / p. 1372) has opined that the use of designations "Practicing Company Secretary", Company Secretary in Practice" or "Company Secretary in Whole-time Practice" by members in practice would not offend section 7 of the Act. Accordingly Guidance Note on Code of Conduct of Company Secretaries stands amended.

However, use of designations like Company Law Consultant, Corporate Law Advisor, Corporate Advisor, Investment Advisor, Management consultant in prohibited. All professionals are assumed to have a particular level of competence and, therefore, it would be only proper for a client to know the member by his proper designation, namely Company Secretary shall not be used, unless there is a specific recognition conferred to any other description or letters.

Renewal of Certificate of Practice (Reg.10)

The certificate of practice issued to a member is required to be renewed every year by payment of annual certificate fee which presently is Rs.200/- and the annual membership fee which presently is Rs.225 for an Associate member and Rs.300 for a Fellow member. The annual certificate fee and the annual membership fee become due and payable on first of April every year and are required to be paid on or before 30th June.

Cancellation of Certificate of Practice (Reg.11):

(1) The certificate of practice shall be cancelled when:

(a) the name of the holder of the certificate is removed from the Register of Members; or

(b) the Council is satisfied that such certificate was issued on the basis incorrect, misleading or false information provided by the applicant or by mistake or inadvertence on the part of the Council, or

(c) the member has ceased to practice; or

(d) the member has not paid the annual certificate fee on or before thirtieth June of that year.

However before canceling the certificate under clause (b) reasonable opportunity to explain his case shall be given to member.

(2) The cancellation of a certificate shall be effective.

(a) in a case falling under clause (a) of sub-regulation (1) from the date on which and during the period for which the name of the holder of the certificate was removed from the Register of Members; and

(b) in any other case, from such date and for such period as the Council may determine.

(3) When a certificate is cancelled, the date from which and the period for which the certificate shall stand cancelled shall be communicated in writing by registered post to the member concerned at the address entered in the Register and may also be published in the Institute's journal 'Chartered Secretary'.

Restoration in Certificate of Practice:

The certificate of practice would be renewed in the same financial year in which it was due for renewal provided the fee for renewal has been received and accepted by the Institute in the same financial year. But, where the certificate of practice was required to be cancelled on failure to pay the annual fee for

certificate of practice on or before the due date prescribed and an application for restoration of certificate of practices has been received and accepted by the Institute in the same financial year the certificate of practice would be restored on payment of the requisite annual fee for certificate of practice for the current year and a restoration fee or Rs.50/-. Where the certificate of practice has not been renewed or accepted for renewal in the same financial year, and as a result of which it was required to be cancelled, a fresh certificate of practice will be issued with effect from the date of acceptance of application for the issue of fresh certificate. A communication for restoration / re-issue of certificate of practice will be sent to the member in writing and may also be published in the Institute's Journal 'Chartered Secretary'.

Certification by Practising Company Secretary:

The Company Secretaries Act, 1980 has conferred statutory recognition to members of the Institute of Company Secretaries of India to engage in practice as company secretaries. Following this, various other Acts, Rules and Authorities have accepted the concept of 'company secretary in practice' and have recognized the right of such secretaries to issue certificates for various purposes. For instance, recognition has been granted to practicing company secretaries for certification of certain documents by, among others, the Public Financial Institutions, State Financial and Industrial Development/Investment Corporations, Indian Banks Association, Chief Controller of Imports and Exports (for the purposes of Import and Export Policy) as well as under the Companies Act, 1956 SEBI Guidelines, Income-tax Act and Rules, M.R.T.P. Act and Regulations, and various other statutes and rules.

Recognitions for Company Secretaries in Practice under the Companies Act and Regulations:

1. Secretaries in whole-time practice recognized under the Act for making declarations for the following purposes:
    a. Section 33(2) – declaration of compliance in connection with the incorporation of a company.
    b. Section 149 – statutory declaration of compliance in connection with commencement of business, where the company ahs not appointed a secretary.

c. Under Proviso to Section 161(1) of the Act, secretaries in whole-time practice are recognized to sign the Annual Return of a company whose shares are listed on a recognized stock exchange. [However, the Council of the Institute of Company Secretaries of India has, vide Notification ICSI No.2 of August, 1989, specified that a member of the Institute in practice cannot sign Annual Returns of more than 30 companies in a calendar year commencing from 1st January, 1989, this becomes operative for any annual return to be signed on or after 1st October, 1989.

d. To certify that requirements of Schedule XIII have been complied with regard to statutory guidelines for appointment of managerial personnel and payment of managerial remuneration to them without the approval of the Central Government [Sec. 269(2) and Schedule XIII)

e. To certify as correct, all documents to be filed by companies Registrar of Companies such that these documents could be taken on record by the ROC with in 10 days (reasonable period).

f. Company secretaries in whole-time practice recognized for filing necessary declaration in respect of companies seeking licence under section 25 of the Companies Act, 1956.

g. To certify in Form 1 that the whole of the amount remaining for a period of 3 years from the date of transfer to the special account u/s. 205A (1) and (2) has been transferred to the Central Government.

h. To act as authorised representative before the CLB benches.

Following recognitions have also been secured for a Secretary in whole time practice.

(i) Making a verified declaration in Form 19 appended to the Companies (Central Government's) General Rules and Forms, 1956 for obtaining a certificate of commencement of business [sec.149 of Companies Act, 1956].

(ii) Making a declaration under Regulation 4 (ii) of the Companies Regulations, 1956 that the Memorandum and Articles of Association have

been drawn up in conformity with the provisions of the Act and that all the requirements of the act and the rules made there under have been duly complied with in respect of registration of matters incidental or supplementary there, in corporation with the formation of sec.25 company.

The Working Group on the Redrafting of the Companies Act has made important recommendation with regard to Secretarial Compliance by companies. Accordingly, companies having paid-up capital in excess of Rs.10 lakhs but less than Rs.2 crores would be required to submit the Secretarial Compliance Certificate would be made optional in respect of companies having a paid-up capital of less than Rs.10 lakhs. The Working Group suggested the Secretarial Compliance report in order that the work of the ROC is reduced to a considerable extent, acting on a report which is certified by a Company Secretary in practice.

Another important area where Company Secretarial has immense potential for growth is financial services. With the establishment of new institutions like CRISIL, NSE, OTCEI, SHCIL, public and private sector mutual funds, company secretaries can play a meaningful role in assisting them in their activity and in carrying out a right place for themselves.

Some of the Working Group's Committees recommendations like introduction of hybrids derivatives and options, provision for buy-back of shares, establishment of Indian Depository Receipts, adequate corporate disclosures, merger of inter-corporate loans and inter-corporate investments, corporate restructuring, corporate governance have thrown up challenging tasks and opportunities for the profession of Company Secretary.

Other Services:

Services Under the Wealth Tax Act:

- Valuation of stocks, shares, debentures, etc.

Services under the Income-Tax Act:

- Acting as an authorised representative before the Income-tax authorities during assessment proceedings, furnishing of records / documents / explanations called for, filing of appeals, claiming refunds, getting the transactions registered.
- Computation of tax payable, filing of returns of income of the company and its directors, obtaining permanent account number, computation and payment of advance tax.
- Advising computation of deduction of tax at source, filing of forms, issue of TDS Certificates.
- Tax planning and tax management for the company – advising about the tax concessions / incentives / reliefs; planning for setting up of business, amalgamation, diversification, expansion to avail tax benefits.

Services under the Competition Law / Consumer Protection Act:

- Acting as an authorised representative before the MRTP Commission / Consumer Forums.
- Advising company on dealership agreements, trade Practices, sales promotion schemes, marketing and sales campaigns.

Financial Services/ Services under the Securities Contract (Regulation) Act/ SEBI Guidelines for Disclosure and Investor Protection:

- Issuing certificate with respect to promoters' contribution.
- Issuing Compliance Certificate to be forwarded to SEBI by the lead merchant banker along with his report on the issue.
- Countersigning certificate to be furnished by the listed company to SEBI to the effect that the terms and conditions for the issue of bonus shares as laid down in the SEBI Guidelines have been complied with.
- Securities Transfer Agents
- Registrar to the Issue

- Share and Stock broker
- Drafting of prospectus / letter of offer / other issue related documents and obtaining various approvals in association with the lead merchant banker.
- Listing of securities on recognised stock exchange.
- Issue advisor / consultant.
- Financial consultant.
- Preparation of project reports for banks and financial institutions.
- Negotiations for financial assistance with banks and financial institutions.
- Raising of funds from international markets through Euro Issues.
- Arranging and advising on industrial licensing, foreign collaborations, joint ventures and setting up of subsidiaries in India and abroad.

Services under the Central Excise Act:

- Acting as an authorised representative before the Central Excise Authorities, Adjudicating Officers or Appellate Tribunal.
- Valuation and classification of goods and correct assessment of duty / obtaining refunds.
- Complying with formalities for the removal of excisable goods.
- Drafting replies to show cause notices issued by the department.
- Advising clients in relation to searches, seizures, etc.
- Set off of duties through various input duty relief schemes.

Services under the Customs Act:

- Acting as authorised representative before customs officers and the Appellate Tribunal.
- Assisting in clearance of import / export classification of goods.
- Valuation of goods and assessment of customs duty and obtaining refunds, if any,

- Documentation and compliance of their formalities.
- Availing duty exemptions and drawback benefits.

Services under the Trade Marks Act:

- Acting as registered Trade Marks Agent.
- Advising on passing off/infringement matters.

Services under the Exports & Imports Policy and Procedures:

- Advising on import / export regulation.
- Issue of various certificates under the Export and Import Policy & Procedures. An illustrative list of certificates is as under:-
  - o Certification of year wise value of the applicant's sales turnover of ammunition (indigenous or imported) during the last three years for obtaining licence for import of ammunition.
  - o Certification of past consumption of the items sought to be imported during the preceding two licensing years with respect to import of other restricted items.
  - o Certification of exports of products manufactured by the applicant in the preceding three licensing years with respect to grant of Export Promotion Capital Goods (EPCG) Licence.
  - o Certification of receipt of sale proceeds of foreign exchange in respect of exports made for each of the three financial years / during the preceding financial year as specified in the statement of exports and in respect of exports for which sale proceeds have not been realized, that the time limit for net realization of sale proceeds has been extended by the RBI with regard to grant of Export / Trading / Star Trading Houses Certificate.

Professional Misconduct:

Section 22 of the Company Secretary Act, 1980 does not provide a clear definition of 'professional misconduct'. It merely lays down that the expression 'professional misconduct' shall be deemed to include any act or omission

included in the First and Second Schedules to the Act. Thus, the definition given in section 22 is only illustrative and not exhaustive.

The concept of 'professional misconduct' needs to be properly understood in order to comprehend its true sense. It does not merely mean non-performance or default in performance of duty by a professional. In essence, it means a failure on the part of the professional to act honestly and reasonably, in addition to the failure to perform the duty. An extract from a judgment delivered by the Calcutta High Court may be quoted to elucidate the concept:

> "Professional misconduct' on the part of a person, exercising one of the technical professions, cannot fairly or reasonably be found merely on a finding of a bare non-performance of a duty or some default in performing it. The charge is not one of inefficiency, but misconduct and in allegation of misconduct, an imputation of a certain mental condition is always involved .... I think the test must always be whether, in addition to the failure to do the duty, partial or entire, which had happened, there had also been a failure to act honestly and reasonably".

Contents of the First and Second Schedules to the Act:

The acts and omissions which would constitute a 'professional misconduct' on the part of a member of the Institute are enumerated in the First and Second Schedules to the Company Secretaries Act. The First Schedule is divided into three parts and the Second Schedule into two parts. The different parts of the two schedules deal with the following:

First Schedule :Part I - Professional misconduct in relation to members in practice.
Part II- Professional misconduct in relation to members in Service.
Part III-Professional misconduct in relation to members in General.

Second Schedule : Part I - Professional misconduct in relation to members in practice requiring action by a High Court.

Part II-Professional misconduct in relation to members in General requiring action by a High Court.

Review Questions :

1. What are the conditions to be fulfilled by a Company Secretary in practice? [C.S. Dec. 1996]
2. Explain the concept of self-regulatory administration. [C.S. June 1997]
3. Define 'secretary in whole-time practice' and state the circumstances in which a member of the Institute of Company Secretaries of India is deemed to be in practice. [C.S. Dec. 1999]
4. Explain the various areas of practice exclusively given by the statute to the practicing Company Secretaries.
5. Discuss the emerging areas of practice for practicing Company Secretaries.
6. What is professional misconduct?

* * *

LESSON 2

SECRETARIAL AUDIT

Objective:

After reading this lesson, the students should be able to under stand the significance of Secretarial Audit, objectives and scope of secretarial audit, appointment and powers of secretarial auditor and checklist in respect of secretarial audit:

Learning Activities:

Reading of

i. **Secretarial, Securities and Management Audit**
by Dr.V.Balachandran & K.S.Ravichandran
Bharath Law Book House, New Delhi

ii. **Master Guide for Company Secretaries**
by S.Kannan, Taxmann Publishers, New Delhi

iii. **ICSI Study Materials**

After reading this lesson the students will be in a position to understand the following:

- Need for Secretarial Audit:
- Objectives of Secretarial Audit:
- Secretarial Auditor:
    - Appointment:
    - Period of Audit:
    - Qualifications:
    - Reporting:
    - Time Limit for Submission of Report:
    - Disqualifications:
- Checklist:

- Incorporation of a Company:
  - Name Availability
  - Preparation of Memorandum and Articles of Association of the Company
  - Articles of Association
  - Filing of the above documents along with requisite registration and filing fees.
  - Obtaining of Certificate of Incorporation
  - Filing of Prospectus or Statement in lieu of Prospectus in respect of public limited Companies.
  - Obtaining of Certificate of Commencement of business in case of public limited Companies.
- Effect of Certificate of Incorporation:
- Change In The Status Of The Company: Private To Public
- Conversion Of Deemed Public Companies Into Private Companies:
- Verification Of Charges
- Meaning of Charge and Creation / Modification / Satisfaction of Charge:
- Modification Of Charge:
- Meaning And Scope Of Modification Of A Charge:
- Analysis Of The Words "Terms And Conditions":
- Analysis Of The Words "Extent Or Operation":
- Satisfaction of charge:
- Kinds of Charges:
- Effects of floating charge:
- Object of Registration:
- Public Notice:
- Effect of Non-Registration:
- Conditions which makes a charge fit for registration
- Charges required to be registered
- Charges not required to be registered
- Relevant Statutory Provisions
- Date of Notice of Charge:
- Transfer of Property Act:

Introduction:

The concept of secretarial audit has been gaining momentum over the last ten years. With the passage of time and its demands on the corporate bodies, one frequently comes across various kinds of audits, in addition to financial audit, both internal and external and the new terminologies are "Proprietary Audit", "Business Audit", "Management Audit", "Legal Audit", "Energy Audit" and of course "secretarial Audit".

The concept, presently in the embryonic stage, needs to be crystallised before any statutory or semi-statutory colour is given. Depending on the agreed and approved scope and area of operation, the professionals in the fields and the institute of company secretaries can provide the Department of Company Affairs with a concrete and properly dressed up proposal leaving the subject to be given final touches by the department by the department. There are at present very few companies in India, which have undertaken such secretarial or legal audit. This is more to suit the demands of a particular company on a particular issue and not done on a regular on-going basis. Today's need is not ad hoc but a continuing in nature.

Need for Secretarial Audit:

Company Secretaries are the only professionals who have the necessary exposure and expertise in various laws and procedures applicable to companies including those governing issue and transfer of securities. In fact, the ICSI is the only professional body in India, which imparts extensive training and education to its members in share transfer laws and procedures. Even in the Company Secretaries Act, 1980, it is specifically provided in section 2(2)(c)(v) that a company secretary in practice may act as a secretarial auditor / consultant. Securities audit is noting but part of the secretarial audit and is, therefore, core area of practice of company secretaries.

The secretarial audit, similarly, if done by an outside authority, a firm of Company Secretaries in Whole-time Practice, is likely to result in routing examination. Outside agency having no or very little personal stake in a company will conduct the secretarial audit in a copy books manner. In the process, many of the subjects inherent to legal and secretarial problems will be given a backseat and only the formal compliance like certification, checking the

statutory books and registers, etc., will take priority. Examination of such books and registers, etc., will take priority. The external auditor always does examination of such books and registers in any event. Under the circumstances, it is doubtful, whether any meaningful purpose will be served by having these registers checked twice – a cosmetic arrangement.

Objectives of Secretarial Audit:

1. It is a pre-emptive audit which seeks to monitor and ensure compliance of various laws.
2. It is expected to deal with procedural and legal compliances that are expected from my company.
3. It would result in qualitative improvement and would save valuable time and resources for the companies.
4. This audit would facilitate borrowing from the financial institutions which generally ask for placing at board meetings of compliance certificates.

Appointment of Secretarial Auditor:

Appointment:

Secretarial Auditor shall be appointed by the Board of Directors from among the secretaries in practice as defined in section 2(2) of the Company Secretaries Act, 1980. In the case of new companies, the appointment can be made at the first meeting of the Board of Directors.

Period of Audit:

The Secretarial Audit would relate to the financial year of the company.

Qualifications:

Only a member of the Institute holding a certificate of practice can be appointed as a Secretarial Auditor.

Reporting:

The secretarial auditor shall submit his report to the Board of Directors. At the option of the company the Secretarial Audit Report may be circulated to shareholders as the Directors' Report.

Time Limit for Submission of Report:

The secretarial auditor is required to submit the report within 90 days from the close of the financial year of the company.

Disqualifications:

(a) None of the following shall be qualified for appointment as secretarial auditor of a company:

   (i) a body Corporate;

   (ii) an officer or employee of the company;

   (iii) a person who is a partner, or who is in the employment of an officer or employee of the company;

   (iv) a person who is indebted to the company for an amount exceeding ten thousand rupees, or who has given any guarantee or provided any security in connection with the indebtedness of any third person to the company for an amount exceeding ten thousand rupees;

   (v) any person who ceases to be a Company Secretary in practice before submitting his Secretarial Audit Report.

(b) A person shall also not be qualified for appointment as secretarial auditor of a company if he is, virtue of the above provisions, disqualified for appointment as secretarial auditor of any other body corporate which is that company's subsidiary or holding company or a subsidiary of that company's holding company, or would be so disqualified if the body corporate were a company.

(c) If a secretarial auditor becomes subject, after his appointment, to any of the disqualifications specified herein above he shall be deemed to have vacated his office as such.

Prior to accepting the appointment, a company secretary in practice shall give a declaration to the company in the prescribed form that he is a Company Secretary in practice as defined in Section 2(2) of the Company Secretaries Act, 1980, and that he does not suffer from any disqualifications set out in the guidelines.

Depending on the size of a company and its problems, perhaps one may take an in between situation that a company smaller in size and operation being unable to afford its own infrastructure may appoint an outside agency to conduct is secretarial audit job, whereas large houses or even comparatively bigger units will find it more useful and profitable to have its own in-house legal / secretarial audit.

If the secretarial audit is restricted only to the provisions of the Companies Act, the work can be entrusted to a firm of Company Secretaries in Whole-time Practice, but when one envisages in larger horizon in the scope of operation of secretarial audit, it may not be practically possible for an outside party to conduct enlarged audit and to frame policies and guidelines for matters beyond the limited scope of the Companies Act. For example, an outsider may not find it easy to conduct legal audit on a regular ongoing basis, to find out whether all the units, divisions and departments are conforming to the respective laws applicable to them, or to ensure that a particular legal matter in a court of law is being properly handled, or even to ensure that the company does not invite MRTP probe in its trade practices.

The objective will be well achieved if the secretarial audit's bigger responsibilities are given to an in-house setup with adequate suitable qualified professionals with the leader of the team being a business manager first and a business manager last. It is only the business manager who can understand the business operations and feel where the shoe pinches and can take corrective and proactive actions. On many occasions, decisions have to be taken, keeping the business interests of the organisation as prime consideration, and, in the process, a company may set its foot on grey areas here and there. The in-house auditor, keeping the company's business interest in mind, can take care of the grey areas, whereas, an outside agency will feel satisfied just to point out the question marks.

The in-house secretarial auditor should demonstrate dogged intransigence in achieving results in keeping up to the expectations, trust and confidence reposed on him by the board of directors. He should not be cowed down or browbeaten by any individual who may not like him to go on with his independent work. Such auditor must not also suffer from fear psychosis and must never make compromise with his professional excellence. He should be

regarded as a valuable possession having rich knowledge of the subject. He must not be a negative manager but, on the contrary, he should find ways and means to fulfill the business needs within the parameters of law.

Checklist:

While undertaking Secretarial Audit / Consultancy, as required, the following should be examined carefully:

1. Memorandum and Articles and Association (Extent of applicability of Table A)
2. Certificate of incorporation
3. certificate of Commencement of Business
4. Annual Reports
5. Minutes Books of Board / Committee / General Meeting
6. Register of Members / Debenture holders
7. Register of Directors
8. Register of Investments
9. Register of Charges
10. Foreign Register of Members and Debenture holders, if any.
11. Copies of Annual Returns
12. Register of Contracts
13. Register of Directors' Shareholdings
14. Register of Loans
15. Share of Transfer Books
16. Correspondence with the Department of Company Affairs, Registrar of Companies, MRTP Commission, Ministry of Industry, Stock Exchange, etc.
17. Listing Agreement with the Stock Exchange.

Incorporation of a Company:

The important steps which are general to incorporation of private and public limited Companies are:

Step 1: Name Availability

A Company is identified only by its name. Further Section 13(1)(a) of the Companies Act, 1956, the Memorandum of Association of the Company should state its name. An application has to be made to concerned Registrar of Companies in the prescribed form (being Form 1 –A as per The Companies (Central Governments) General Rules & Forms, 1956 along with a fee of Rs.500/-). The promoters are also given an option to suggest 3 other names in addition to the name for which the name availability is sought. This is to enable the promoter to seek name availability if either first preferred name is not made available due to technical reasons. The principles which governs the availability of name is

A Company will not be allowed to use a name which is prohibited under the Emblems & Names (Prevention of Improper Use) Act, 1950. Section 2 & 3 read with Schedule under The Emblems & Names (Prevention of Improper use) Act, 1950, provides for names, emblems, official seal which are prohibited for adoption by Companies. For e.g., The name, emblem or official seal of the United Nations Organisation, World Health Organisation etc, Indian Flag etc. The Department of Company affairs also devised guidelines for deciding availability of names, some of major guide lines which govern name availability are:

(a) That it is not in consonance with the main objects of the Company as set out in its Memorandum and Articles of Association of the Company.

(b) That the words comprised in the proposed name are offensive to any Section of public.

(c) That the proposed name has a close phonetic resemblance to the name of a Company in existence.

(d) The proposed name is too general.

(e) The proposed name connotes government patronage or includes the word "Co-operative or its equivalent in the regional languages of the Country or includes the name of a national hero or a person held in high esteem or importance.

Further depending on the authorised capital of the proposed Company or an existing Company the Department has listed certain key words for e.g:

(a) The word Corporation can be used only if the authorised capital is Rs.5 Crores.

(b) The words International, Globe, Universal, Continental, Inter-continental, Asiatic, Asia used as first name required an Authorised Capital of Rs.1 Crore. If these words are used in a bracket then the authorised capital required is Rs.50 Lacs.

(c) The words Hindustan, India, Bharat used as first word then the authorised capital required is Rs.50 Lacs. If these words are used within brackets then the authorised capital required is Rs.5 Lacs.

(d) The words Industries / Udyog required authorized Capital of Rs.1 Crore.

(e) The words enterprises, products, business, manufacturing requires authorised capital of Rs.10 Lacs.

Further the applicant should state in brief the main objects of the Company proposed to be incorporated for which name availability is sought. The name should reflect the main business that the Company will pursue on incorporation. For e.g. The name ABC Pumps Private Ltd will suggest to the public that the Company is involved in manufacture of pumps. Whereas the name ABC Motors Private Ltd would suggest that the Company is involved in the manufacture of motors which is a wide term than pumps and includes pumps also.

Thus a promoter seeking the name ABC Pumps Private Ltd, cannot include in its main objects for the manufacture of Car engines etc since the word `pumps' will refer a machine used for pumping liquids like water, oil etc. Hence the promoter should first decide upon the objects which his proposed Company will pursue on incorporation and should accordingly coin the name of the Company. It is always advisable to have a name of wider import which will include varied objects so that the promoter is saved from the pain of changing the name at a latter stage for better identification when the Company diversifies into a different product area.

If the Registrar is satisfied that the name availability which is sought for is clear of restrictions imposed by the Emblems & Names (prevention of Improper use) Act, 1950 and guidelines issued by the Department of Company Affairs then the Registrar will make available the name for adoption by the applicant. The period for which the name will be made available is 6 months from the date of sanction. If the promoter is unable to incorporate the Company for which the name was obtained should renew the availability of the name by submitting a fresh Form 1-A with a fee of Rs.500/-.

Step2: Preparation of Memorandum and Articles of Association of the Company

(a) Memorandum of Association:

✓ Name Clause – Should be as per name availability letter.

✓ Situation Clause - Should be the name of the state in which the Company is proposed to be incorporated.

✓ Objects Clause

- Main Objects – As per the main objects specified in the Form 1A filed for obtaining availability of name.
- Ancillary or Incidental Objects
- Other objects

✓ Capital Clause – Authorised Capital of the Company:

- As per Section 3 (1) (iii) of the Companies (Second Amendment) Bill, 1999, a "Private Company" means a Company which has a minimum paid-up capital of one lakh rupees or such higher paid-up capital as may be prescribed, and by its articles –

(a) restricts the right to transfer its shares, if any;

(b) limits the number of its members to fifty not including –

  (i) persons who are in the employment of the Company; and

  (ii) persons who, having been formerly in the employment of the Company, were members of the Company while in that employment and have continued to be members after the employment ceased; and

(c) prohibits any invitation to the public to subscribe for any shares in, or debentures of, the Company:

(d) prohibits any invitation or acceptance of deposit from persons other than its members, directors or their relatives.

Provided that where tow or more persons hold one or more shares in a Company jointly, they shall, for the purposes of this defination, be treated as a single member.

- As per Section 3 (1) (iv) of the Companies (Second Amendment) Bill, 1999, a "Public Company" means a Company which –

  (a) is not a private Company;

  (b) has a minimum paid-up capital of five lakh rupees or such higher paid-up capital, as may be prescribed;

  (c) is a private Company which is a subsidiary of a Company which is not a private Company.

✓ Liability Clause – Stating the liability is limited or unlimited

(b) Articles of Association

In case of a private Company it is better to draft articles since application of majority of the provisions of the Companies Act is exempted for a private limited Company.

In case of a public Company, the provisions of table A to Schedule I of the Companies Act , 1956 can be adopted in to.

(c) **Form No.32** – First Directors of the Company

(d) **Form No.29** – Relating to undertaking to act as a Director – required only in case of public limited Companies.

(e) **Form No.18** – Specifying the address of Registered Office of the Company.

(f) **Form No.1** - Declaration by a Company Secretary / Chartered Accountant / Cost Accountant / Advocate entitled practice in High Court or Supreme Court / Director of the proposed Company stating that all the requirements of the Companies Act, 1956 and the rules made there under have been complied with in respect of registration.

(g) Name availability in original

Step 3: Filing of the above documents along with requisite registration and filing fees.

Filing Fees

Authorized Capital	*New Fee*	*Old Fee*
Less than Rs.1,00,000/-	Rs.100/-	Rs.30/-
Rs.1,00,000/- or more but less than Rs.5,00,000/-	Rs.200/-	Rs.60/-
Rs.5,00,000/- or more but less than Rs.25,00,000/-	Rs.300/-	Rs.100/-
Rs.25,00,000/- or more	Rs.500/-	Rs.120/-

Authorized Capital	New Registration Fee	Old Registration Fee
Upto Rs.1,00,000/-	Rs.4,000/-	It was in a slab manner but for Rs.1,00,000/- it was Rs.1,500/-
For Rs.5,00,000/-	Rs.16,000/-	Rs.5,500/-
For Rs.10,00,000/-	Rs.26,000/-	Rs.8,500/-
For Rs.25,00,000/-	Rs.56,000/-	Rs.14,500/-
For Rs.50,00,000/-	Rs.1,06,000/-	Rs.22,000/-
For Rs.1,00,00,000/-	Rs.1,56,000/-	Rs.37,000/-
For every Rs.1,00,00,000/- above the first Rs.1,00,00,000/-	Rs.50,000/-	Rs.30,000/-

As per Notification No.SO 658(E), Dated 12-7-2000, issued by the Department of Company Affairs, Ministry of Law, Justice & Company Affairs –

In exercise of the powers conferred by sub-section (1) of Section 614 of the Companies Act, 1956 (1 of 1956), the Central Government hereby makes the following amendment to Schedule X of the said Act, namely –

(i) Under Schedule

Fee Payable on Registration of Capital Increase Thereof X, the existing paragraph 1.3 shall be read as under:

"For filing a notice of any increase in the nominal share capital of a Company, the difference between the fees payable on the increased share capital on the date of filing the notice for registration of Company and the fees

payable on existing authorised capital, at the rates prevailing on the date of filing the notice".

Step 4 : Obtaining of Certificate of Incorporation

Step 5 : Filing of Prospectus or Statement in lieu of Prospectus in respect of public limited Companies.

Step 6 : Obtaining of Certificate of Commencement of business in case of public limited Companies.

Effect of Certificate of Incorporation:

A Certificate of Incorporation gives a conclusive evidence that all the requirements of the Companies Act, 1956, have been complied with in respect of registration and matters precedent and incidental thereto. But this does not mean that a Company with an illegal object can pursue such objects after incorporation.

Change in the Status of the Company: Private to Public

(a) By operation of Law (Section 43A) – Deemed Public Company:

- ✓ Where not less that 25% of the paid up share capital is held by a public limited Company.
- ✓ Where not less than 25% of the paid up share capital of a public limited Company is held by private limited Company.
- ✓ Where average annual turnover of a private Company during period of 3 consecutive financial years is not less than Rs.25 Crore.
- ✓ Where a private Company accepts deposits by invitation.

(b) By Volition (Section 44):

By passing a special resolution at the Annual General Meeting for removing the provisions of Section 3(1)(iii) from the Articles and a resolution for deletion of the word Private from the name of the Company.

(c) By default (Section 43):

Private Company fails to comply with three restrictive provisions under Section 3(1)(iii) then the Company ceases to be a private Company and also ceases to enjoy the exemptions conferred by the Act as a private Company and it becomes the public Company and all the provisions of the Act become applicable to it.

(d) As per sub-clause 11 of the Companies (Second Amendment) Bill, 1999 has been added to Section 43A of the Act. As per the said sub-clause –

"Nothing contained in this section shall apply on and after the commencement of the Companies (Second Amendment) Act, 1999".

Conversion Of Deemed Public Companies Into Private Companies:

(i) Convene a general meeting for passing a special resolution for conversion of the deemed public Company to private Company and the consequent insertion of the word "Private" in the name of the Company.

(ii) If the Articles of Association of the Company does not contain the restrictions applicable to a private limited company as contained under Section 3 (1)(iii) of the Act, a special resolution is required to be passed for inserting such restrictions.

(iii) File Form No.1B along with the following:

- a) Form No.23 along with the certified copy of resolution and explanatory statement.
- b) A certified extract of minutes of the extra-ordinary general meeting.
- c) Certified copies of Annual Report for the past three years, if the Company seeks re-conversion on the basis of not failing the turnover test.
- d) To obtain the certificate from Registrar of Companies for the re-conversion of the company into a private Company and fresh certificate of incorporation consequent to name change.

Verification of Charges

The Companies Act, 1956 is a lengthy piece of legislation providing for maximum disclosure of various particulars by companies. Broadly categorised, there are private and public companies. The Act has offered a host of privileges to private companies, as the scope of public interest in such companies is very restricted.

The objects of these provisions are to safeguard public interest. Corporate business entities function out of moneys of public, collected directly in the form of shares etc, or indirectly in the form of borrowings from banks and institutions.

Every business organisation borrows. Borrowing is a common and very basic activity that it could be called as BLOOD SUPPLY to a business organisation.

Corporate borrowers have an additional but statutory obligation to intimate the Government about borrowings, whenever such borrowings are secured by some of the properties of the borrowers. Elaborate and stringent provisions have been made to ensure strict compliance of these provisions and thus serve the object of these provisions. These provisions constitute a major problem for the lenders and the borrowers and also the Registrar of Companies.

While there has been sincere attempts from the Government side to simplify the existing procedures and thus solve the ills associated with this matter, it must be the endeavour of all concerned to understand the scheme of the Act, the purpose of such disclosure, the object of registration, the reasons for delay thereof, the consequences of non-filing of the particulars etc.

Part V of the Companies Act, 1956 (hereinafter the Act) contains provisions in respect of charges on properties of a company beginning from Section 124 to Section 145 of the Act. The Companies (Central Government's) General Rules and Forms, 1956 provides certain procedural formalities as regards filing and registration of particulars of charges, modification of charges, and satisfaction of charges. This chapter of the Act has always been a strong area of practice for professionals such as chartered accountants, cost

accountants and company secretaries and to certain extent lawyers also. Even though these provisions have been administered for more than four decades, there are certain areas where views differ from a person to another. Even professionals adopt different ways of filling up of forms. Difficulties exist in identifying whether a particular transaction constitutes a modification to an existing charge or is that a fresh charge.

Meaning of Charge and Creation / Modification / Satisfaction of Charge:

The word "Charge" has not been defined under the Companies Act, 1956. Section 124 merely says it includes mortgages. Various court judgments have tried to explain the meaning of "Charge".

It is very difficult to define the word 'Charge'. At best, it could be indicated by explanation. The word is commonly used in association with ELECTRICITY. When an electric current is applied on a particle, it said to have been charged. In the context of the present discussion, a charge is said to be created when as security for repayment of a debt the borrowers extend any of their properties with an intention to give a legal right to the creditor to have the security made available to him on he happening of an event, i.e. a default.

While as a matter of general rule in almost all borrowings, charges are created, we are concerned about corporate borrowers and the statutory provisions with regard to the charges created by such borrowers.

Filing and registration of particulars of a charge created by a company are important in view of the fact that if the prescribed particulars of a charge are not filed with the Registrar of Companies in the prescribed manner the charge becomes void against the liquidator and any creditor of the company in so far as any security on the company's property or undertaking is conferred thereby. From the above language of Section 125 of the Companies Act, the focus, in so far as compliance of the provisions of this Part (other than those relating to satisfaction of charges) is concerned, gets shifted from the company to the charge holder. It is the imperative duty of every charge holder and the statutory duty of every company to understand the legal consequences and file the

particulars of charges / modification of charges in the prescribed manner so as to avoid litigations at a later stage.

Modification of Charge:

During the period the loan remains outstanding and the charge still subsists, any change in the extent or operation of the charge, say, enhancement / revision of facility, change in interest rate, change in the nature or extent of security etc., would amount to modification. Particulars of a modification of a charge must also be intimated and filed to the Registrar of Companies as and when it happens.

Meaning and Scope of Modification of a Charge:

Section 135 of the Act provides that whenever the terms or conditions, or the extent or operation, of any charge registered under this part are or is modified, it shall be the duty of the company to send to the Registrar the particulars of such modification, and the provisions of this part as to registration of a charge shall apply to such modification of the charge.

Though the above section is very obtuse in describing as to what would constitute a modification to a charge it gives a clue as to the circumstances under which it shall be the duty of a Company to send to the Registrar the particulars of a modification. In other words the rule laid down by the said section for determining as to whether a particular transaction constitutes a modification of a charge or not is to be understood only by analysing in depth the meaning of the words "terms or conditions, or the extent or operation " used in the opening sentence of the section.

As per the said section, a charge stands modified whenever all or any one of the following particulars of a charge are or is modified.

i. Terms of an existing charge or conditions subject to which the said charge was created or is in existence.

or

ii. Extent of an existing charge or operation of an existing charge.

Analysis Of The Words "Terms And Conditions":

The words "terms" and "conditions" generally refer to the terms of repayment of the loan / limits for the securing of which the charge was created, the rate of interest on the amount secured, the margin etc. It may also include the term (period) for which the sanctioned limit is valid.

As per the Webster's Encyclopedic Unabridged Dictionary of the English language, the term "terms" means:-

a. The conditions with regard to payment, price, charge, rates, wage etc.
b. Conditions or stipulations limiting what is proposed to be granted or done.

Further a charge, in general, operates as security not only for the amounts advanced but also for interest and other charges thereon. Hence any change in these terms / rates is considered as an occasion requiring the filing of particulars of modification of a charge.

Analysis Of The Words "Extent Or Operation":

As per the said dictionary, the word "extent" means the space or degree to which a thing extends; length, area, volume or scope. Thus where there is a change in the scope of a charge, it is deemed to be a modification of the charge.

As per the said dictionary, the word "operation" means the act or an instance, process or manner of functioning or operating. Thus where there is a change in the factors determining the operation of the charge, it constitutes a modification.

Thus the test to determine as to whether a subsequent transaction has or has not the effect of modifying a charge already in existence is to be carried out on the basis of the facts associated with the case under reference. If the subsequent event has the effect of resulting in any change in the terms or conditions pertaining to the existing charge or if it has the effect of resulting in any change in the extent or operation of the existing charge, then such subsequent event ought to be filed only as a modification to the existing charge.

Satisfaction of charge:

Section 138, 139 and 140 of the Companies Act, 1956 deal with matters relating to satisfaction of charges. Section 138 requires the Company to report the satisfaction of charge. The Registrar has been empowered to take note of the satisfaction of charge on evidence being given to the satisfaction by a source other than the concerned Company as per the provisions contained in Section 139. The Registrar of Companies, under Section 140, has to furnish to the Company a copy of the memorandum of satisfaction.

Kinds of Charges:

Floating Charges on movables includes stock in trade. It is created on existing as well as those acquired in the course of business. Subject matter of the charge undergoes constant change from time to time. It does not settle down and fasten.

Specific Charge fastens on definite and ascertained property or property capable of being defined and ascertained.

A fixed/specific charge is made against an asset which is ascertained and definite or is capable being so ascertained at the time the charge is created – for e.g. land, building or heavy machinery. A fixed charge therefore is against the security of a specific property and the company loses the right to dispose of that property as unencumbered. In other words, the Company can deal with such property, subject to the charge so that the charge holder gets priority over all subsequent transferees except a bonafide transferee for consideration with notice of earlier charge. In the winding up of a Company, a debenture holder secured by a specific charge will be placed in the highest ranking class of creditors.

A floating charge is ambulatory shifting in nature hovers over.

What converts a floating charge to a fixed charge?

(i) Borrower defaults and charge holder intervenes.
(ii) Borrower ceases his business.

Effects of floating charge:

A floating charge created within 12 months immediately preceding the commencement of winding up of a company is invalid.

Object of Registration:

Public Notice:

Serves as an effective notice to those who intend giving loans to companies, whether the object is secured? No. Why? How can the position be remedied.

It also could prevent false claims at the time of Liquidation.

Effect of Non-Registration:

(i) Void against liquidator / against creditors, but against them only.

(ii) Charge good against Company. Amount becomes payable immediately.

(iii) All remedies are available to charge holder as long as Company is going concern.

(iv) Subsequent creditor if registers charge, he gets priority.

(v) If not registered, on liquidation charge holder ranks as unsecured.

(vi) Holder of equitable mortgage has no lien on title deeds.

(vii) Though charge is void, it does not affect contract to repay.

(viii) Non-registration invites penalty on Company and officers of Company.

Conditions which makes a charge fit for registration

(i) After 01/04/1914

(ii) Created by Company

(iii) Registerable as per Section 125

(iv) On Company's property

Charges required to be registered

(i) Security for loans to other companies / firms / concerns.
(ii) Property acquired subject to charge.
(iii) Conversion / take over of partnership / proprietorship.
(iv) Leasehold rights i.e. buildings.

Charges not required to be registered

Unpaid vendor, bailee by order of Court, pledge of movables deposit receipts, pro notes are not charges as per Section 125 of the Act. They are exempt as possession is parted with the pledge. Of course filing of particulars of a charge created by pledge of movables and registration of the same is permitted though not mandatory.

The registration by the Registrar of a charge being a pledge on the movable property of a Company, though not mandatory, is permissible at the instance of the company or of any interested person, provided the latter files the necessary particulars with the prescribed filing fee. The Registrar should, however, point out to the party concerned that such registration is not statutory compulsory but would be made by him `without prejudice', if the party insists on the Registrar registering the charge. The Registrar should also simultaneously advise the party seeking registration of the charge that in that case it would be in the company's own interest if particulars of any subsequent modification of the charge and of its satisfaction are duly intimated to the Registrar.

Circular:No.8/6(125)/60-PR, dated 7th July, 1960.

Relevant Statutory Provisions

1. The Companies Act, 1956
2. Section 17 of the Registration Act, 1908
3. Section 58(a) of Transfer of Property Act, 1882
4. Rule 6 of the Companies (Central Government's General Rules and Forms, 1956.

Section 126:

Date of Notice of Charge:

On and from the date of Registration, any person intending dealing with charged property shall be deemed to have notice of charge.

Section 127:

Property acquired subject to a charge – take over of Partnership

Section 128:

Charge t• the benefits of debenture holders.

Section 129:

Commission on debentures to be issued.

Section 130:

Register of Charges – Form No.13

Section 131:

Index to the Register of charges.

Section 132:

Conclusive evidence of requirements.

Section 134:

Duty of the Company to file with Registrar of Companies for registration - Right of Interested persons.

The Transfer of Property Act:

Section 58(a)

Mortgage means Transfer of an Interest in specific immovable property –

(a) for securing the payment of money advanced or to be advanced by way of loan.

(b) an existing of future debts.

(c) or the performance of an engagement which may give rise to a pecuniary liability.

Section 59 of the Transfer of Property Act:

(i) Where the mortgage is not by deposit of title deeds;

(ii) Where the principal money secured is Rs.100/- or more;

(iii) It can be effected only by a registered instrument;

(iv) It should be signed by the mortgagor;

(v) Attested by two witnesses.

* * *

Review Questions

1. What is meant by Secretarial Audit? What are its objectives?
2. Who can be appointed as Secretarial Auditors? State their qualifications.
3. State briefly the meaning and scope of 'secretarial audit report' [C.S. Dec. 1997].
4. While undertaking secretarial audit, what are the books and documents that have to be examined carefully? [C.S. Dec. 1997]
5. You are appointed as secretarial auditor of X Ltd. How would you commence the audit and which of the data and records would you examine? [C.S. Dec. 1996]
6. Explain the duties and powers of Secretarial Auditors?
7. Discuss the need for and scope of Secretarial Audit?
8. List out the areas which a secretarial auditor is normally expected to examine and comment in his audit report.[C.S. Dec. 2000]

LESSON – 3

SEARCH AND STATUS REPORTS

Objective:

After reading this lesson, the students should be able to under stand the concept of search and status reports, their significance, verification of documents relating to charges, requirements of various financial institutions and other corporate lenders, the format of search report.

Learning Activities:

Reading of

i. **Secretarial, Securities and Management audit**
by Dr.V.Balachandran & K.S.Ravichandran
Bharath Law Book House, New Delhi

iii. **ICSI Study Materials**

After reading this lesson, the students should be able to under stand the following:

- Meaning:
- Definition:
- Verification of Charges:
- Compilation of Search Report:
- Certificates to Financial Corporations / Institutions
- Certificate of Adequacy of Insurance to be Submitted Every Half Year:
- Certificate / Statement showing the Value of Fixed Assets and Other Assets Mortgaged or Charged to the Corporation and Sources Thereof:
- Copies of Resolutions Passed at Company Meetings to be Furnished to Financial Institutions:
- Format of Certificate of Adequacy of Insurance
- Format of Search Report:

Meaning:

The term search involves the physical inspection of documents and the term status indicates the reporting of information as made available and gathered from the inspection. The search and status report provides information on the charges created in favour of other lenders which helps a lender to assess the total exposure of a company and also helps lenders to aforesee where it could stand if the company were to go into liquidation.

Definition:

A search and status report can be defined as a report furnished based on the information gathered by a search of specific records made available for inspection in a public office and reporting of the same form as they are recorded or registered in the said public office or in any other convenient form.

A corporate entity presupposes a large undertaking with a number of shareholders and other creditors including banks and financial institutions. In India, even after the liberalisation of the economic policy of the economic policy of the government, most of the banks and financial institutions are in the public sector. Thus public interest is all pervasive and requires enough protection. These banks and other institutions, whether in the private or public sector acquire a stake in the corporate entities by lending monies for their projects. The money is lent by them, either for setting up of a project or for working capital purposes, in addition to the equity or other long-term capital of the promoters and other share / debenture holders and other lenders form the source of capital.

When these lenders, by lending and thereby participating in the project or business of companies, acquire a peculiar right in the company as a matter of security. A said right is acquired when a company pledges or hypothecates or mortgages its assets. Under the companies act the right acquired by any person when the properties, present or future, tangible or intangible, movable or immovable of a company is pledged or hypothecated or mortgaged is called a charge. A charge stands created when a company pledges or hypothecates or mortgages its properties in favour of one or more lenders. The lenders, thus, secure their money by requiring the assisted companies to create a charge on their properties.

Verification of Charges:

The search and status report acts a tool to confirm and evidence certain information. In order to gather any specific data or information a search has to be conducted at the office of the Register of Companies where in accordance with the provisions of the act, the companies are required to file some documents and returns. Thus the agency is generally the practicing company secretary, the source is the documents and returns filed by the companies at the office of Register of Companies, the report primarily contains on status of charges and secondarily other material particulars and the beneficiary of such reports is the lender.

The concept of verification of charges does not stop with a mere reproduction of the particular of charges in the form of search and status report as they are available in the records maintained by the Registrar of Companies but requires –

- a thorough study of the particulars relating to the amount secured by the charge and the terms and conditions governing the charge;
- an analysis of the security available to a particular lender for its advances;
- a comparison of charges created in favour of a particular lender vis-à-vis other lenders;

Compilation of Search Report:

For taking inspection of the Register or documents at Registrar's office, it will be primarily necessary to know the number of the concerned Company as given in the concerned Registrar's office. This number will normally be the same as given in the certificate of incorporation if the company has not transferred its registered office to another state. In the latter case, new number will be given by the Registrar upon which transfer. If the company number is not known, it will have to be enquired with the client or at the Registrar's office.

Search Report compiled on the basis of the scrutiny of the above documents at the ROC's office is, therefore, related and restricted to only those

documents which are filed in Document File and are available for the inspection on the date(s) when the search is carried out.

Meticulous care will have to be taken in noting down the following particular from the Register of Charges and the Document File:

(a) Date of registration (preferably with the serial number) of the document
(b) Date and nature of the document creating the charge
(c) Amount of the charge
(d) Brief particulars of the property charged
(e) Name and address of the person n whose favour the charge is created.

In respect of each of the charges created, it would be essential to identify the modifications effected form time to time by noting down carefully the following particulars:

(a) Date of registration (preferably with serial number) of the document
(b) Date of satisfaction.

Certificates to Financial Corporations / Institutions

The All-India Financial Institutions while granting term loans to companies insist on certain formalities to be completed by a company availing such loan. These include furnishing of certificates by company secretaries in practice in regard to the following:

a) Necessary power of a company and its directors to enter into an agreement.

b) Borrowing limits of a company under section 293(1)(d) of the Companies Act, 1956, including details of share capital – authorised, issued, subscribed and paid-up and the actual borrowing.

c) List of members of a company.

d) Certificate regarding exemption to proposed borrowing under the capital issues (exemption) order, 1969.

e) Copies of resolutions passed at company meetings to be furnished to financial institutions.

The financial institutions require that this certificate will have to refer to the relevant clause(s) of the Memorandum of Association of the company, which gives specific powers to the company and to secure the repayment of the same by mortgage, charge, lion, etc. the opinion will also have to refer to the relevant article(s) of the Article of Association and the general body resolution, if any, under which the board of directors are authorised to borrow or raise moneys, secure the repayment thereof and execute on behalf of the company, bonds, deeds, documents, etc.

Certificate of Adequacy of Insurance to be Submitted Every Half Year:

The IFCI (vide their letter extracted) has recognised certificate from accompany Secretary in Practice in regard to adequacy of insurance to be submitted every half year viz. on 30th June and 31st December. Before giving the certificate it is necessary to verify the original insurance policies and check carefully the details of properties covered by the policy. Particular attention shall be paid to note (ii) in the 'Statement of Insurance Cover' and if that clause is applicable, the certificate should clearly give an explanatory statement.

Certificate / Statement showing the Value of Fixed Assets and other Assets Mortgaged or Charged to the Corporation and Sources thereof:

The IFCI recognises the certificate in respect of the above to be given by a Company Secretary in Practice. The format of the certificate is given. A study of the format suggests that the particulars in the statement have to be wholly taken from the books of the company. Hence in respect of each of the items in the statement, the Company Secretary in practice shall look for authentic entry in the books / documents maintained by the company.

Copies of Resolutions Passed at Company Meetings to be Furnished to Financial Institutions:

A company secretary in practice has been recognised to certify resolutions passed at company meetings. As per letter from the IFCI copies of the following resolutions can be certified by a Company Secretary in Practice.

1. Resolution to be passed by the company in general meeting in pursuance of section 293(1)(d) of the Companies Act, 1956.
2. Ordinary revolutions to be passed by the company at the general meeting under section 283(1)(a) of the Companies Act, 1956.
3. Resolutions to be passed at a meeting of the Board of Directors of the borrower for acceptance of the terms and conditions of letter of intent and execution of documents.

Format of Certificate of Adequacy of Insurance

CERTIFICATE

Dated ....

The ED/GM/DGM/AGM/Manager

IDBI/IFCI/ICICI

....

Dear Sir,

We have verified the insurance policies taken by M/s.. for its plants located at ....
and certify that the insurance policies are in the joint names of the Institutions, viz., IDBI / IFCI / ICICI / UTI / IRBI / Banks as the mortgagees and the Company / Society as mortgagers. The details of the policies and the coverage vis-à-vis the value of assets are given in the enclosed statement duly signed by us.

Yours faithfully,

(Auditors)

Encls.: Statement as above

Chartered Accountants.

Format of Search Report:

Search Report
on
The Charges of the Assets of
_______________________________________ Limited
(Company Number ________________________)

I/We have carried out the search of the Register of Charges and the documents relating to the charges on the assets of the above named Company as registered by and available for inspection on ___________ at the office of Registrar of Companies ____________________ and hereby report that the following particulars of charges in respect of the above-named Company have been so registered:

Sl. No.	Date of registration	Instrument creating charge and date	Amount of charge Rs.	Short Particulars of property charged
(1)	(2)	(3)	(4)	(5)

Name & address of Person in whose Favour the charge Is created	Particulars of Modification		
	Date of registration	Instrument modifying the charge	Effect of modification
(6)	(7)	(8)	(9)

Notes:

(1) The figures in bracket in column numbers 2 and 7 indicate the serial numbers under which the respective documents have been registered.

(2) The last document registered in the Document File and available for inspection at the office of Registrar of Companies, ______________________________

(3)

(4)

____

(Signature with Seal)
Name and Address of
Company Secretary in
Practice: ________

Place:________
Date:________

Certificate of
Practice No:____________
Membership No.__________

* * *

Review Questions

1. What is meant by search and status report?
2. Explain the objectives of preparing a search and status report.
3. State the important points to be considered while preparing a search and status report.
4. Mention the essential matters to be certified by a Company secretary in respect of borrowings by a company from the IDBI as regards the following:
5. Borrowing powers of a company: and
6. Borrowing powers [C.S. June 2000].

7. A financial institution is in the process of granting a loan to Needy Ltd. and in this connection you have been engaged to prepare a status on the borrowings and charges created. Explain the work involved in this regard. [C.S. June 1999].

8. Discuss the contents of status/search report prepared by a company secretary in practice. [C.S. June 1998].

9. You have been approached by a financial institution to obtain a status report on the borrowings made and charges created by A L Ltd. to whom the financial institution wishes to grant loan. Discuss the work involved in this regard. [C.S. Dec. 1996].

10. What are the documents to be prepared in connection with Search and Status Report?

LESSON – 4

SECURITIES AUDIT

Objective:

After reading this lesson, the students should be able to under stand the objectives and significance of Securities Audit, Scope of the Securities Audit, preventing fraudulent and unfair trade practices & benefits of securities audit:

Learning Activities:

Reading of

i. **Secretarial, Securities and Management audit**
   by Dr.V.Balachandran & K.S.Ravichandran
   Bharath Law Book House, New Delhi

ii. **SEBI Practice Manual, by VL.Iyer**
   Taxmann Publications, New Delhi

iii. **ICSI Study Materials**

- Objectives of Securities Audit:
- Significance of Securities Audit:
- Scope of Securities Audit
- Legal Framework:
- Benefits of Securities Audit:
- Benefits to investors
- Company Secretary is the ideal Professional:
- Certifications by the issuer or by other professionals:
- SEBI (Prohibition of Fraudulent and unfair Trade Practices relating to Securities Market) Regulation,1995":
- Listing of Securities:
- Vanishing Companies:
- The Depositories Act, 1995
- Dematerialization of securities:
- Transfer of securities under the Depository mode:
- Dematerialization or defungification of securities:

Introduction:

Securities Audit is an important requirement in the era electronic paperless issue, trading and settlement of securities of the corporate world. One would feel that if only 'Securities Audit' had been in vogue as a statutory requirement, many cases of fraud in the capital market involving crores of rupees, investor grievances, delay in completion of various transactions relating to securities, failure to pay declared dividends, vanishing promoters, switching of shares and so many such violations, acts of omissions and commissions would not have occurred at all. Under the Companies Act, 1956, shares are of two kinds viz., Preference Shares and Equity Shares. Apart from those shares one would also see the word debentures finding place in the said Act. The term securities would cover with its ambit shares of different kinds, instruments of various kinds convertible into shares, debentures and such other instruments by whatever name called which are issued by companies for raising medium and long term resources for meeting the financial requirements of the company.

1 It is significant that the need for Securities Audit was felt even four decades ago. As far back as in 1957, the Companies Act Amendment Committee (Visvanantha Sastri Committee) considered introduction of a share transfer audit. The committee observed:

"It has been brought to our notice that some companies do not keep a proper record of their share transfer and sometimes even issue certificates without reference to such transfers. Some companies have however, a share transfer audit, a practice which. We consider is commendable, but which we do not think can be made compulsory at this stage. It is, in any case, desirable to provide that the management should certify, when making an annual return, that a proper record of such transfers has been maintained. We recommend the addition of a new clause (c) to sub-section (2) of section 161 in these terms:

(c) That since the date of the last annual return, the transfer of all shares or debentures and the issue or debentures and the issue of all further certificates have been properly recorded in the books maintained for the purpose: [Para 66 of the Report]

1.1 While the aforestated recommendation of the Companies Act, 1956, the Companies (Amendment) Act, 1988, went a step ahead and took the first step towards introduction of the Secretarial Audit. The Companies (Amendment) Act, 1988, has introduced a provision that the Annual Return filed by a company whose shares are listed on a recognised stock exchange should be signed by a Secretary in Whole-time Practice, in addition to the other signatories, who are officers of the company [Proviso to section 161(1)]. It is pertinent to note that one of the major (and voluminous) contents of the Annual Return is "particulars regarding members and debentures holders, past and present" of a company, which include transactions of transfer of shares / debentures.

1.2 In its report the group set up by the SEBI headed by C.B.Bhave, Sr. Executive Director, SEBI, to look into the problems relating to the transfer of shares by companies, observed: SEBI was established with the twin objectives of protecting the interests of the investors in securities and regulating and promoting the development of the securities markets. Redressal of the grievances of the investors is an important part of SEBI's activities towards its first objective, i.e. protection of the interests of the investors. From the past experience, it is noted that a large number of complaints are received from the investors against the companies and the companies relate most of them to the transfer of shares. It was felt that there was a need to study the problems relating to transfer of shares for necessary reforms. The group observed that with the growth of the capital market in the country, there is significant increase in the listing of securities, number of investors and in the trading activity on the stock exchanges. All these factors have given rise to an unprecedented increase in the transfer of shares of companies and have led to generation of tremendous paper work. In this increased activity of transfer of shares, there are a variety of problems faced by the investors, stockbrokers and companies. The recommendations of this group are set out as Annexure I.

1.3 In an approach paper submitted to the SEBI Chairman, D.R.Mehta on December 4, 1995 the Institute of Company Secretaries of India (ICSI) has suggested introduction of the Securities Audit in the case of listed companies by Company Secretaries in Whole-time Practice with a view

to curbing fraudulent and unfair practices in relation to securities and for better investor protection.

MEANING OF THE WORD "SECURITIES" AS USED IN THE RELEVANT STATUTES AND ITS DICTIONARY MEANING

According to "Webster's encyclopedic unabridged dictionary":

i. Security means freedom from danger, risk and safety.

ii. Freedom from care and apprehension.

iii. Something that secures or makes safe and protection.

iv. Freedom from financial cares or from want.

v. Law – something given or deposited as surety for the fulfillment of a promise or an obligation.

According to "The Law Lexicon" by Shri.P.Ramanatha Aiyer, the word "Securities" means, in the context of this discussion, documents entitling the holder to specified realizable rights in land, money, stocks, shares, bonds, mortgages, etc. It also denotes documents entitling the holder to specified realizable rights in land, money, stocks, shares, bonds, mortgages etc.

A careful reading of the above meaning in the context of the topic under discussion it would appear that the word connotes the existence of a duty and obligation on the part of the assuring party, namely the issuer of securities and the confidence conveyed to the assured, namely the investor.

But the word "securities" has been defined in different ways in different statutes. In order to understand the legal meaning, it is necessary to go through the definition given under certain legislations. Securities and Exchange Board of India (SEBI) was constituted under the Securities and Exchange Board of India Act, 1992 for protecting the interests of investors in securities and to promote the development of, and regulate, the securities market and for matters connected therewith or incidental thereto. A mere reading of the preamble of the said Act would suggest the important role SEBI is expected to play in the interests of the investors and in regulating the securities market. Even the said Act refers to the

definition of the word "securities" contained in the Securities Contracts (Regulation) Act, 1956.

As per the Securities Contracts (Regulation) Act, 1956,as amended by the Securities Laws (Amendment) Act, 1999 that came into force w.e.f 22/02/2000, the word "Securities" include –

(i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

(ii) Government securities;

(iia) such other instruments as may be declared by the Central Government to be securities; and

(iii) rights or interests in securities.

(iv) Coupons.

While the word "Government Security", as per the said Act, means a security created and issued, by the Central Government or a State Government for the purpose of raising a public loan and having one of the forms specified in clause (2) of Section 2 of the Public Debt Act, 1944 (18 of 1944), the words shares, scrips, bonds, debentures and other marketable securities are of very common in nature and they have to be understood in the context of the Companies Act and other relevant statutes.

Another interesting feature of the amendment in the year 2000 is the insertion of a definition for the "derivative" which connotes a hybrid variety of securities introduced by the corporates in the modern world to suit the needs of the project financials and the investor preferences. As per the said Act the word "derivative" includes a security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security.

In fact the word "debentures" do not find any precise definition anywhere in the said Act or the Companies Act, 1956.

Finding a precise definition for the word "Debenture" is very difficult. The Law Lexicon of Shri.P.Ramanatha Aiyer has the following to say.

"Debenture" is a word which has somehow crept into the English Language, and does not appear to admit any accurate definition, but it is recognized by the statute as something different from a promissory note." [*British India & c.Co.v.Commissioners of Inland Revenue* (1881) 7 Q.B.D 165, 170].

"A debenture means a document which either creates a debt or meaning of the word "SECURITIES" as used in the relevant statutes and its dictionary meaning

According to "Webster's encyclopedic unabridged dictionary":

1. Security means freedom from danger, risk and safety.
2. Freedom from care and apprehension.
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"A debenture means a document which either creates a debt or acknowledges it, and any document which fulfils either of these conditions is a debenture." [*Levy v. Abercorris Slate, & c. Co* (1887) 37 Ch.D.260, 264, Chitty, J., where the derivation and history of the word is discussed acknowledges it, and any document which fulfils either of these conditions is a debenture." [*Levy v. Abercorris Slate, & c. Co* (1887) 37 Ch.D.260, 264, Chitty, J., where the derivation and history of the word is discussed.

Objectives of Securities Audit:

Securities Audit would essentially act as a pre-emptive check to monitor the compliances relating to issue and transfer of securities. It would help in –

(i) Ensuring proper compliance of provisions relating to issue and transfer of securities.

(ii) Ensuring that the investors are serviced as per law and are not taken for a ride.

(iii) Creating awareness among companies about the need for complying with the various provisions of law, listing guidelines, administrative instructions issued by SEBI, Government and other regulatory agencies from time to time.

(iv) Providing mechanism for self-regulation by companies and instill professional discipline.

(v) Relieving the Company and its directors from the consequences of unintended non-compliance by timely corrective action.

(vi) Preventing fraudulent and unfair trade practices.

(vii) Protecting the interest of investors.

Significance of Securities Audit:

The purpose of or the need for carrying out a securities audit is manifold. It ensures that the Company has complied with the all the provisions of the various Acts, rules, regulations, directions and guidelines so that the officers responsible for such compliance are put to serious trouble by the law enforcing agencies. It also helps the Company in ensuring that the securities issued by the Company have duly issued and properly accounted. Such audit eliminates the chances of fraud in dealing with securities. The Company need not be concerned about the possibility of the Company distributing dividend and other entitlements such as bonus and rights to persons who are not entitled for such benefits.

It is possible, while auditing the securities of a Company with lakhs and lakhs of individual investors, to come across some instances, probably due to unintentional mistakes on the part of the people entrusted with the responsibility of ensuring issue of securities in a proper way, such as issue of securities to persons to whom such issue ought not to have been made or to send refund of moneys received by the Company in excess of the amount required to be retained by the Company for number of securities issued and allotted. Such a situation will not arise if there is proper audit procedure to ensure that the systems in place with the Company for issue of and dealing in securities have been scrupulously followed and there has been no transgression in any area

irrespective of the investor. This audit also protects the Company from the possibility of loss or theft while handling blank certificates of title to securities.

As far as the investors are concerned this audit ensures at the first instance proper procedure for speedy disposal of grievances of investors. Such a machinery, if set up in a Company, would help the management of the Company to redress the grievances of the investors to great extent saving the Companies from the severe penal mechanism built in the SEBI Act and other legislations. Further after a reasonable length of time, the audit would gradually reduce grievances totally and the Company may be able to become a zero grievance Company.

The securities audit has much more things to do. It not only helps the Companies and investors but also the Government agencies involved in protecting the question of interests of investors. Such agencies will be relieved from the burden of receiving and attending to various grievances of the investors. In many cases, the grievances may be minor in nature if the amount invested taken as an indicator of the seriousness of the grievance. But from the point of view of the investor, such grievance may be an agonising experience and if the Government were to deploy its human and other resources in settling the minor grievances of investors, it would drain the exchequer heavily on the one side and deprive the Government of considerable time and energy which otherwise could deployed by such agencies in investigating large scale frauds connected with issue of dealing in securities.

Further the said audit if properly understood and carried out by trained professionals could prevent grievances, frauds and consequential litigations arising out of such grievances and frauds. This will go a long way in reducing the number of cases pending adjudication in various Courts and quasi-judicial forums.

The Securities Scam is an excellent example of the possibility of scams of such magnitude to take place in spite of the availability of a plethora of laws, rules, regulations, guidelines, orders, instructions and directions. Moreover the need for investigating such frauds and money and other resources that are being spent by various agencies could be avoided if there is in place a fool proof audit system. Such an audit system can take the responsibility of ensuring a smooth

issue and dealing in securities relieving, as a whole, the Company, the investors, the Government agencies and the Courts.

Scope of Securities Audit

The Securities Audit would involve checking of the registers, records, documents, etc. concerning shares / debentures of a Company or its share transfer agent with regard to issue, allotment and transfer / transmission, consolidation, sub-division, etc. thereof. It would also involve verification concerning extra-ordinary matters such as forfeiture and re-issue of forfeited shares, conversion of debentures, warrants and other securities into shares, reduction or reorganisation of capital on amalgamation, redemption of preference shares or debentures or re-issue of redeemed preference shares, etc. In its approach paper submitted the SEBI, the ICSI has recommended:

"The Scope of Securities Audit would include a report to SEBI / Regional Stock Exchange by a Company secretary in practice on –

(a) whether requirements in relation to issue of shares and debentures have been complied with and the share / debenture certificates have been issued within the prescribed time;

(b) whether the transfer of shares and debentures and the issue of share certificates thereof have been made within the stipulated time and in accordance with the procedure prescribed;

(c) whether the Company has circulated the annual accounts, directors' and auditor's reports as per the provisions of the Companies Act / listing agreement;

(d) whether the Company has disbursed the dividend declared by it within the stipulated time to the members and has paid interest on debentures issued by it on due dates;

(e) whether the unclaimed dividends have been transferred to the General Revenue Account of the Central Government and intimation sent to members about the dividend unclaimed;

(f) whether the Company has appointed debenture trustees and executed debenture trust in the manner prescribed and credited debentures

redemption fund for the redemption of debentures; whether the redemption of debentures has been made as per the terms of issue;

(g) whether the Company has issued refund orders in respect of excess application money or unsuccessful applicants within the stipulated time;

(h) whether the amount received on applications has been refunded in full within the prescribed time, if minimum subscription has not been received and the issue has failed;

(i) whether the Company has furnished the requisite information to stock exchange, from time to time, as required under the listing agreement;

(j) whether the requirements of Stock Exchanges, administrative instructions issued by SEBI, Department of Company Affairs, Department of Economic Affairs (Stock Exchange Division) have generally been complied with;

(k) whether the Company has devised suitable mechanism to attend to investor complaints".

The scope of securities audit is very wide. It varies from Company to Company. It depends on the size of the Company, the number of investors, the kinds of securities, the nature of the instruments issued / proposed to be issued by a Company, the state of the securities, meaning in physical form or dematerialized form or partly in one form and partly in another form, the terms if issue of securities, conversion option, the software in use and the hard ware equipments deployed by the Company in handling securities, the quality of man power employed by the Company, the support of professionals, both internal and external, the financial position of the Company, the arrangement the Company has with various agencies who are required to be appointed as intermediaries at the time of issue, their reputation and standing in the field and the capacity and efficiency of the Registrars and Transfer Agents for handling the post issue obligations of the Company.

Legal Framework:

Transactions in securities of listed bodies corporate encompass a plethora of statues, rules, and regulations, guidelines issued by several authorities. Some of these are:

- The Companies Act, 1956.
- The Companies (Issue of Share Certificate) Rules, 1960.
- The Securities Contracts (Regulation) Act, 1956.
- The Securities & Exchange Board of India Act, 1986.
- The Monopolies & Restrictive Trade Practices Act, 1969.
- The Foreign Exchange Regulation Act, 1970
- The Indian / State Stamp Acts,
- Rules, Regulations & Guidelines issued by SEBI and Stock Exchanges.
- Listing Agreement.

Benefits of Securities Audit:

Benefits to the nation / law-enforcing authorities / stock exchanges:

a) Building-up investor confidence in the securities market.

b) Effective regulation of the securities market.

c) Better compliance with laws, rules, regulations, etc.

d) Better investor protection.

e) Detection of and remedial action against irregularities, malpractices, frauds, unfair practices, such as insider trading.

f) Stricter enforcement of listing agreement.

g) Achieving the objective of healthy and orderly development of the securities market.

h) Avoiding discreditable events such as scams, scandals, malpractices and thereby saving the country's securities market from disgrace and loss of confidence.

i) Avoiding loss of revenue on account of stamp duties on transfers and certificates, fees, etc.

Benefits to Investors

a. Instilling professionalism.

b. Effective control and monitoring of Registrar and Transfer Agents' activity.

c. Detection of delays, irregularities, malpractices, frauds, etc. committed by the people handling work relating to securities either in house or outside agencies.

d. Winning and nurturing investor confidence and thereby gaining reputation as 'investor friendly' Company.

d. Improving and strengthening quality and speed of investor sector.

e. Avoiding disputes, litigation by investors and law-enforcing agencies.

Company Secretary is the ideal Professional:

Company Secretaries in Whole-time Practice are already involved in the certification of annual return of the listed companies under section 161 of the Companies Act. They are the members of the ICSI and undergo stringent education and training requirements of the ICSI to be eligible to function as Company Secretaries. The ICSI is a reputed statutory body and is known for high standards of its examinations and training of its members. It, through its headquarter, four regional offices and 36 chapters all over India, regularly conducts professional development activities with a view to enhancing knowledge, expertise and skills of its members. Membership of the ICSI is the only qualification recognised for a person to act as Company Secretary (both in practice and in employment).

Number of certifications are required to be given to the Stock Exchange in which the security is proposed to be listed and to the SEBI. These certifications are:

- that allotment has been made as per the basis approval by Stock Exchange
- in respect of preferential allotment where lock-in period is applicable, that the related share certificates have been stamped indicating that

such shares shll not be sold / transferred / hypothecated for the stated period

- compliance certificate relating to promoter's contribution to be brought before opening of public issue towards subscription of shares / convertible instruments as the case may be.

Certifications by the issuer or by other Professionals:

- certificate by the Merchant Banker and the Chief Executive / Company Secretary to be effect that the issue has been subscribed at least upto 90% of the total issue – at the time of getting Stock Exchange's approval for the basis of allotment.
- In the event of under subscription, the issuer has to confirm to the Stock Exchange that the balance has been taken up by the underwriters or their nominees as per their liabilities for the short fall.
- A certificate from the Bankers to the issue indicating the number of applications and the amount of application money received and that all applications have been delivered to the company.
- A certificate from the Auditors to the effect that the expenditure on the public issue has not exceeded the prescribed ceilings.

The issuing company is required to confirm / furnish the following to the Stock Exchange after the issue is closed:

- the Stock Exchange to be advised as the list is closed
- detailed listing application, its execution.
- arrangements for receiving allotment money at all centres where applications were received
- five copies of Analysis Forms.
- the date of completion of posting of letters of allotment / certificates to be intimated as well as that of refund orders.
- register of members / debenture holders are open for registering transfers.

- distribution schedules to be filed in duplicate with Stock Exchange.
- the company should keep the Stock Exchange posted with the progress of receipt of applications form the Bank with details regarding number of applications, number of securities applied for, number of applications rejected, valid, number of securities applied for by eligible applicants, subscriptions received as a percentage of capital offered, distinctive numbers of securities to be listed.
- Cutting of newspapers in which announcement was made and the basis of allotment, in case of over-subscription was published.
- Statement of region wise money remitted and statement in the prescribed format to the Stock Exchange about the money received.

SEBI (Prohibition of Fraudulent and unfair Trade Practices relating to Securities Market) Regulation,1995":

This regulation notified by SEBI on 25.10.1995,seeks to cover market manipulation on stock exchanges as well as practice like wash sales, front running, price rigging and artificially increasing and decreasing price of securities. The guiding principles of the regulations are that a market would function efficiently only if those seeking to disturb its equilibrium and generate false signals are prohibited from during so and the wrongdoers are punished. The regulations specify the practices which could be considered fraudulent and unfair.

Listing of Securities:

Listing of securities in one or more recognized stock exchanges is pre-requisite for Issue of securities to public. As per Section 73 of the Companies Act, 1956, every Company intending to offer share or debentures to the public for subscription by the issue of a prospectus shall, before such issue, make an application to one or more recognised stock exchanges for permission for the shares or debentures intending to be so offered to be dealt with in the stock exchange or each such stock exchange.

Sub-section (1A) of the Section 73 of the said Act provides that the names of stock exchanges to which the Company has made an application for

the securities of the Company to be dealt in should also be given in the prospectus and any allotment made on an application in pursuance of such prospectus shall, whenever made, be void, if the permission has not been granted by the stock exchange or each such stock exchange, as the case may be, before the expiry of ten weeks from the date of the closing of the subscription lists.

The purpose of the said statutory provision requiring the listing of securities issued to public is to provide an opportunity for the investors to sell or buy their securities at market determined prices whenever they may intend to do so. In contradistinction with this requirement, there is no listing requirement in the case of issue of shares and other securities to public made in the garb of "Private Placement" as already stated.

In Union of India V A.I.Products (1971) 41 Com cas 127 (SC), the Supreme Court held that the object of Section 73(1) of the Companies Act, 1956 is that the subscribers to the shares must have facility to approach an Exchange for having their holdings converted whenever they desire. Even if out of several Exchanges approached, one or more, but not all, have granted the application for "enlistment", the facility of ensuring quick conversion is still available. If after representing in the prospectus that an application has been made to a recognised exchange for "enlistment" or will be made with the prescribed period, the Company is unable to obtain permission for "enlistment" from any exchange, the allotment will be invalid. But Sub-section (1) is not intended to mean that it will be invalid, even if permission is obtained, but not from all the Exchanges to which applications have been made.

But in Rishyashringa Jewellery Ltd V The Stock Exchange, Mumbai. 1996) 85 com cas 479 (SC), the Supreme Court, reversing its earlier decision in the 1971 case cited supra, gave a detailed explanation to the expression "each such stock exchange" clarifying that even if one stock exchange refuses to list the securities of a Company, the entire allotment would be void. In the said case the Supreme Court held that Section 73 (1A) required that where a prospectus states that an application under Sub-section (1) has been made for permission for the shares or debentures offered thereby to be dealt in one or more recognised stock exchanges 'such prospectus shall state the name of the stock exchange or as the case may be each such stock exchange'. In other words, if the application is made only to one stock exchange then the name of that stock exchange is to be

mentioned and where the prospectus states that application has been made to more than one recognised stock exchanges then it shall state the name of each such stock exchange, i.e., every such stock exchange or in other words, all the stock exchanges to which the application has been made. The second part of Sub-section (1A) of Section 73 then provides the consequence of refusal to the permission by saying that any allotment made on an application in pursuance of such prospectus shall be void "if the permission has not been granted by the stock exchange or each such stock exchange", as the case may be, before the expiry of ten weeks from the date of the closing of the subscription list. This means that any allotment made shall be void if the permission has not been granted by the stock exchange where the application is made to more than one stock exchanges. The expression "each such stock exchange" here must mean the same as in the earlier part of Sub-section (1A) of Section 73, i.e., each and every or in other words, all such stock exchanges. Thus, where the prospectus held out that enlistment of shares would be in more than one stock exchange the consequence envisaged in Sub-section (1A) of Section 73 ensues to render void the entire allotment of shares unless the permission is granted by each and everyone or all of the stock exchanges named in the prospectus for enlisting the shares. This is the plain meaning of sub-section (1A) of Section 73. In short, unless permission is granted by each or everyone of all the stock exchanges named in the prospectus for listing of shares to which application is made by the Company, the consequence is to render the entire allotment void. In other words, if the permission has not been granted by any one of the several stock exchanges named in the prospectus for listing of shares the consequence by virtue of sub-section (1A) of Section 73 is to render the entire allotment void and the grant of permission by one of them is inconsequential. This construction also promotes the object of insertion of Section 73(1A) by amendment of the law made to overcome the effect of the decision of the Supreme Court in AIR 1971 SC 251.

Thus there have been cases where securities could not be allotted due to refusal by stock exchanges to entertain the application of companies for listing of the securities under issue in a public offer and as a consequence of such refusal the moneys collected had to refunded and in certain cases allotment made have become void. In the said case of the Rishyashringa Jewelry Ltd the allotment letters had already been despatched and the shares have been traded for some time in the other exchanges. By the time Supreme Court decided the case, there were a lot of transfers of shares from one to another. When the

allotment was declared void after the decision of the Supreme Court, the Company was caught in a peculiar situation of having to refund the money collected but not having even a clue as who would be holding the shares on a particular date so that the refund goes to the right person.

Here it is necessary to understand two important things about the capital market. Even before the certificates are issued, shares are traded on the strength of allotment orders and before the details of transfer reaches the Company, the shares in question would have changed hands several times. The transfer forms are, in the case of a listed Company, valid, as per Section 108 of the Companies Act, 1956, for a period of (1) one year from the date of its presentation before the prescribed authority.

Vanishing Companies:

In order to track the vanishing promoters, the Department of Companies Affairs has constituted a high level committee for launching prosecution against them. The SEBI has also banned the appointment of the directors of those vanishing companies in the Board of any Company.

As per Section 11B of the Securities and Exchange Board of India Act, 1992, if after making or causing to be made an enquiry, the SEBI is satisfied that it is necessary –

(i) in the interest of investors, or orderly development of securities market; or
(ii) to prevent the affairs of any intermediary or other persons being conducted in a manner detrimental to the interest of investors or securities market; or
(iii) to secure the proper management of any such intermediary or person.

It may issue such directions to any person or class of persons or associated with the securities market or to any Company in respect of matters relating to issue of capital and transfer of securities as may be appropriate in the interests of investors in securities and the securities market.

As per press release (Ref.No.PR 193/99,) Dated 26-8-1999, issued by Primary Market Department, SEBI, [1999] 21 SCL 333 (st), relating to action taken against vanishing companies and directors, under Section 11B of the SEBI Act, SEBI has already debarred 70 directors for a period of 5 years from associating themselves in any manner with the capital markets. The orders gave such directors, 15 days time to make a representation to SEBI. So far, representations have been received only from 8 directors. SEBI has given opportunity to these 8 directors for a personal hearing to present their case with explanation. Final orders would be issued once the hearing process is completed. In respect of other directors, the orders have already come into effect. The order would mean the directors are prohibited from raising resources from the capital market, deal in securities in any manner and also restricts their association with any capital market intermediary.

The Central Coordination and Monitoring Committee comprising of Secretary, Department of Company Affairs (DCA), Chairman, SEBI and their officials also reviewed the various actions initiated by the 7 task forces constituted for the purpose of tracking violators of provisions of law relating to the issue of securities. Based on the findings of task forces, the DCA has initiated inspection under Section 209A of the Companies Act, 1956 in respect of 25 companies. Various prosecution has been launched in respect of 43 companies by the DCA. Registrar of Companies have also informed the police about the cases where cheating was suspected. The stock exchanges are also initiating various actions like issue of notice of prosecution for failure to complying with the listing provisions, petitions for winding up and other measures.

The said central committee considered the following criteria for identifying defaulting companies:-

a. Companies which have not complied with listing requirements / filing requirements of Stock Exchange / ROC respectively for a period of 2 years.

b. No correspondence has been received by the exchange from the Company for a long time.

c. No office of the Company is located at the mentioned registered office address at the time of Stock Exchange inspection.

Moreover as per press release (Ref. No. PR 123/2000), dated 7-6-2000, issued by Primary Market Department, SEBI [2000] 25 SCL 159 (st), in order to effectively coordinate the actions among the other regulatory authorities, the committee decided to involve, inter alia, RBI, CBDT and Economic Offence Wing / Local Police in the task force depending on the need.

Further DCA agreed to positively consider amending the provisions of Sections 542 and 543 of the Companies Act, 1956 (casting personal liability on defaulting directors) so that the directors of vanishing companies are also prosecuted under the said sections. Action under Section 439 (winding up of companies) and Section 388B (directors declared not fit and proper person to hold office) may also be initiated against defaulting companies / directors.

In fact the offenders are many. What SEBI and DCA have booked appears to be only the tip of the iceberg. Stringent action must be taken in order that the punishment serves as a deterrence and the persons should not be eligible to become directors of any companies. Had there been a thorough pre-issue and post-issue audit of securities, this offenders could have been booked or checked at an early date. Now much water has flown to think of redeeming the confidence of the investors that stands shattered. It is in this context, securities audit assumes significance. What is lacking is not legal provisions but the assurance that an offender is sure of getting penalised in accordance with the provisions of law. It has been decided by SEBI and DCA to refer these cases to respective State Government also for action where cheating or fraud is observed. It was felt that fraud and cheating are the offences under the Indian Penal Code and could have dealt only by the police authorities of the respective State Governments. Besides punishment under the offences are far more severe.

The Depositories Act, 1995

Dematerialization of securities:

This Section lays down the procedure in which the "dematerialization" of the share certificates takes place. This process involves the following steps:-

(i) Entering into an agreement by the shareholder with the participant as provided in the earlier sections;

(ii) Exercise of option of availing of the services of the Depository;

(iii) Surrender of the share certificate to the issuer (i.e. the Company in which the shares are held);

(iv) Cancellation of the share certificate by the issuer;

(v) Substitution of the name of the Depository in the records of the Company in place of the erstwhile shareholder. Thus, the Depository becomes the "registered owner" of such shares;

(vi) Recording of the name of the erstwhile shareholder by the Depository as the holder of such shares. Thus such shareholder now becomes the beneficial owner.

Transfer of Securities under the Depository Mode:

This system comes into operation only when the shares are already held in the Depository system. However, in such a case, if the purchaser does not wish to avail of the Depository system, he can opt for paper share certificates. The procedure of transfer of shares would take a form similar to that of the dematerialization of shares. Whenever there is a transfer of shares, by sale or otherwise, the participant would inform the Depository of the same. The Depository, in turn, would record the name of the transferee as the "beneficial owner" of the shares in place of the transferor.

Hypothecation or pledge of shares and other securities held in the depository mode:

This provision is novel in the realm of corporate law. Hitherto, there was no adequate facility whereby the charge of a person, in respect of shares, could be recorded in the records of the Company. Thus, for example, where a banker had lent money to the shareholder against security of this shares, there was no facility whereby the charge of the banker could be recorded in the Company's registers. This Section now provides for record of any hypothecation or pledge

in the register of the Depository. This will, however, be subject to the regulations and bye-laws that may be made in this behalf.

The beneficial owner, who wishes to create a pledge or a hypothecation in respect of the shares held by him through a depository would have to follow the following procedure:-

1. Ensure that the regulations and bye-laws are duly complied with.
2. The prior approval of the Depository is taken. It is hoped that the approval would be a formality and would not act as a bottleneck in any way to the creation of the charge.
3. After obtaining the approval of the Depository, the beneficial owner shall create the charge and intimate the details thereof to the Depository.
4. On receipt of the details of the charge, the Depository shall make appropriate entries in its records.

The entry in the records of the Depository shall be evidence of a pledge of a pledge or hypothecation.

It may be appreciated that a pledge, which required physical surrender of the security to the lender, would, in any case, have been impossible in the case of shares held through a Depository for the obvious fact of non-existence of the share certificates. This provision overcomes the fact of such non-existence and allows for the creation of the charge nonetheless. One can expect, however, some difficulties in applying the term "pledge" to this situation where the share certificates do no exist physically.

Dematerialization or Defungification of Securities:

It may happen that any shareholder, after having opted (at the time of allotment of shares or at the time of purchase) to hold shares under the Depository system, may decide to have physical possession of the share certificates. In such a situation, he is required to follow the procedure detailed hereunder:-

He shall inform the Depository of his decision to do so.

The Depository, in turn, shall

(a) make necessary entries in his records and
(b) intimate the issuer Company of such a fact.

The Issuer Company shall, on receipt of the prescribed fees from the erstwhile beneficial owner, within thirty days of the receipt of intimation from the Depository, issue the share certificates to such beneficial owner.

Public limited companies proposing to get their shares listed for the first time on a recognised Stock Exchange should contract the Recognised Stock Exchange authorities to understand the requirements for listing. The company should apply for listing its sharesin the prescribed form.

The listing application fromduly filled in and signed and along with the enclosures referred to in the said application should be sent to the Stock Exchange accompanied by the following:

1. Listing agreements duly executed and stamped on a non-judicial stamp paper of requisite value.
2. Initial Listing fees.

The following documents and particulars are to be furnished by a public company while applying for listing it's shares pursuant to Rule 19(1) of the Securities Contracts (Regulation) Rules, 1957.

1. memorandum and articles of association;
2. copies of all prospectuses or statements in lieu of prospectus issued by the company at any time;
3. copies of offers for sale and circulars for advertisements offering any securities for subscription or sale during the last five years;
4. copies of balance sheets and audited accounts for the last five years, or in the case of new companies, for such shorter period for which accounts have been made up;
5. a statement showing-

(a) dividends and cash bonus, if any, paid during the last ten years (or such shorter period as the company has been in existence, whether as a private or public company);

(b) dividends or interest in arrears, if any;

6. certified copies of agreements or other documents relating to arrangements with or between-

   (a) vendors and / or promoters;

   (b) underwriters and sub-underwriters;

   (c) brokers and sub-brokers;

7. certified copy of every letter, report, balance sheet, valuation contract, court order or other document, part of which is reproduced or referred to in any prospectus offer for sale, circular or advertisement offering securities for subscription or sale, during the last five years;

8. a statement containing particulars of the dates of, and parties to all material contracts, agreements (including agreements for technical advice and collaboration), concessions and similar other documents (except those carried on by the company) together with a brief description of the terms, subject-matter and general nature of the documents;

9. a brief history of the company since its incorporation giving details of its activities including any reorganisation, reconstruction or amalgamation, changes in its capital structure, (authorised, issued and subscribed) and debenture borrowings, in any;

10. particulars of shares of the company since its incorporation giving details of its activities including any reorganisation, reconstruction or amalgamation, changes in its capital structure, (authorised, issued and subscribed) and debenture borrowings, if any;

11. particulars of shares and debentures issued –

    a) for consideration other than cash, whether in whole or part;

    b) at a premium or discount; or

    c) in pursuance of an option;

12. a statement containing particulars of any commission, brokerage, discount or other special terms including an option of the issue of any kind of securities granted to any person;

13. certified copies of agreements, if any, with the Industrial Finance Corporation, Industrial Credit and Investment Corporation and similar bodies;

14. particulars or shares forfeited;

15. a list of the highest ten holders of each class or kind of securities of the company as on the date of application along with particulars as to the number of shares or debentures held by and the address of each such holder;

16. particulars of shares or debentures for which permission to deal is applied for;

Provided that a recognised stock exchange may either generally by its bye-laws or in any particulars case call for such further particulars or documents as it deems proper.

Rule 19(2)(a) of the Securities Contracts (Regulation) Rules, 1957 provides that a company before listing its shares shall satisfy the Stock Exchange that its articles of association, inter allia, provide for the following:

(1) that the company shall use a common form of transfer;

(2) that the fully paid shares will be free from all lien, while in the case of partly paid shares, the company's lien, if any, will be restricted to moneys called or payable at a fixed time in respect of shares;

(3) that any amount paid-up in advance of calls on any share may carry interest but shall not entitle the holder of the share to participate in respect thereof, in a dividend subsequently declared;

(4) there will be no forfeiture of unclaimed dividends before the claim becomes barred by law;

(5) that option or right to call of shares shall not be given to any person except with the sanction of the company in general meeting.

Review Questions

1. What is meant by securities audit? Explain the objectives of Securities Audit.
2. What is meant by listing of securities? State the procedure for listing of securities.
3. Explain the need and scope of securities audit.
4. What are the prerequisites of securities audit?
5. What is meant by demat of securities? What are its objectives?
6. State the guidelines for demat of securities sent for transfer by custodians.
7. Write a note on rematerialisation of shares.
8. What is meant by Investor Education and Protection Fund? How is it augmented and utilized?
9. What is meant by de-listing of securities? Under what circumstances is it resorted to?
10. Explain the procedure involved in voluntary de-listing of securities.
11. How securities audit can be a powerful tool for investor's protection?
12. Explain the checklist for conducting securities audit.

LESSON 5

COMPLIANCE CERTIFICATE

Objective:

After reading this lesson, the students should be able to under stand the meaning and significance of **compliance certificate**; *the Companies (Compliance Certificate) Rules, 2001; Obtaining of Compliance Certificate; Scope of Compliance Certificate; Period of Certification; Filing of Compliance Certificate; Methodology for Carrying out Verification for Certification; Certification with Qualification; Penalty for false Compliance Certificate; Checklist with respect to Compliance Certificate; Specimen Compliance Certificate.*

Learning Activities:

Reading of

i. Secretarial, Securities and Management audit
by Dr.V.Balachandran & K.S.Ravichandran
Bharath Law Book House, New Delhi
ii. SEBI Practice Manual, by VL.Iyer
Taxmann Publications, New Delhi
ii. ICSI Study Materials

- The Companies (Compliance Certificate) Rules, 2001:
- Obtaining of Compliance Certificate:
- Scope of Compliance Certificate:
- Period of Certification:
- Filing of Compliance Certificate:
- Right to access Records:
- Attachment of Compliance Certificate with Board's Report:
- Laying of the Compliance Certificate at the Annual General Meeting:
- Penalty for Non-Compliance:
- Disqualifications of Secretary in whole-time Practice:
- Communication to earlier incumbent:
- Methodology for Carrying out Verification for Certification:
- Certification with Qualification:

- Penalty for false Compliance Certificate:
- Professional responsibility:
- Fees for Compliance Certificate:
- Checklist:
- Articles of Association:
- Borrowing Powers:
- Membership of a Company:
- Number and Appointment of Directors:
- Appointment of Managerial Personnel:
- Nomination:
- Rights of a Nominee under Sections 109A and 109B –
- Right to Nomination:
- Rights of the company under Sections 109A and 109B
- Steps to be taken by nominee to register himself as shareholder:
- Transfer Of Shares:
- Checklist for Audit of Transfer Deeds:
- General Meeting
    - Statutory Meeting:
    - Annual General Meeting:
    - Extraordinary General Meeting:
- Declaration of Dividends:

The Companies (Amendment) Act, 2000 has inserted a proviso to Sub-section(1) of section 383A of the Companies Act, 1956, with regard to issue of Compliance Certificate, which reads as follows:

"S.383A(1) Every company having such paid-up share capital as may be prescribed shall have a while-time secretary, and where the Board of directors of any such company comprises only two directors, neither of them shall be the secretary of the company:

Provided that every company not required to employ a whole-time secretary under Sub-section(1) and having a paid-up share capital of ten lakh rupees or more shall file with the registrar a certificate from a secretary in whole-time practice in such form prescribed, as to whether the company has

complied with all the provisions of this Act and a copy of such certificate shall be attached with Board's report referred to in section 217".

As per rule 2 of the Companies (Appointment and Qualifications of Secretary) Rules, 1988, every company having a paid-up share capital of rupees fifty lakhs or more is required to have a whole-time secretary.

Accordingly, every company having a paid-up share capital of rupees ten lakhs or more but less than rupees fifty lakhs is required to file with the Registrar of Companies (ROC) a Compliance Certificate from a secretary in while-tile practice and also attach a copy of that certificate with Board's report.

The Companies (Compliance Certificate) Rules, 2001:

In terms of the newly inserted proviso the Sub-section(1) of section 383A, the Central Government has prescribed the companies (Compliance Certificate) Rules, 2001 (hereinafter called the rules) for issue of Compliance Certificate by a Secretary in wholetime practice (hereinafter referred as CSP).

Commencement of Rules:

The Rules have come into force w.e.f. February 1, 2001 i.e. the date of their publication in the Official Gazette.

Obtaining of Compliance Certificate:

According to sub-rule (1) of rule 3, every company not required to employ a while-time secretary under Sub-section (1) of section 383A of the Act and having a paid-up share capital of ten lakh rupees or more shall obtain a certificate from a CSP.

It may be noted that the requirement of obtaining Compliance Certificate is mandatory for a company to which proviso to sub-section (1) of section 383A applies even if it has employed a whole-time secretary.

Thus, every company which is not required to employ a whole-time secretary and whose paid-up share capital is ten lakh rupees or more at any point

of time during the financial year, shall be required to obtain Compliance Certificate from a CSP in respect of that financial year.

Scope of Compliance Certificate:

The scope of Compliance Certificate would comprise of certification of the compliance of various requirements under the Companies Act and the Rules there under. The CSP should certify compliance only in respect of matters specified in the Form prescribed under the Rules and where any matter is not applicable, he should specify accordingly.

Sub-rule(2) of rule 3 specifies that the Compliance Certificate shall be in Form appended to the Rules or as near therto as circumstances admit. Certain amount of flexibility in the Form has, therefore, been provided which means that if any information required to be given in the certificate does not fit into the format, necessary modifications may be made in the format by the CSP.

At the time of issue of the first Compliance Certificate, CSP should verify the registers and records maintained by the company from the first day of the financial year except where there are reasons for CSP to verify the records for the earlier years. Such occasions may arise in respect of maintenance of registers, retirement of directors by rotation, issue of share certificate when the allotments were made in the earlier years, payment of managerial remuneration, etc.

Period of Certification:

Sub-rule (2) of rule 3 provides that the Compliance Certificate shall relate to the period pertaining to the financial year of the company.

The Companies (Amendment) Act, 2000 has come into force w.e.f. 13th December, 2000 and the companies (Compliance Certificate) Rules, 2001 have come into force w.e.f. from 1st February, 2001. Accordingly every company to which these rules are applicable is required to obtain in Compliance Certificate from a CSP for the financial year in respect of which Board's report is signed on or after 1st February, 2001.

Filling of Compliance Certificate:

Every company to which these rules apply is required to file with the ROC the Compliance Certificate within thirty days from the date on which its annual general meeting is held.

Where the annual general meeting of such company for any year has not been help, such certificate is required to be filed with the ROC should have been held in accordance with the provisions of the Companies Act.

In case the annual general meeting is held and adjourned, the Compliance Certificate should be filed with the ROC within thirty days from the date on which such adjourned meeting was held provided such adjourned meeting is held within the statutory limit.

Right to Access Records:

Sub-rule (3) of rule 3 provides that the CSP for the purpose of issue of Compliance Certificate shall have right to access at all times to the registers, books, papers, documents and records of the company whether kept at the registered office of the company or elsewhere and shall be entitled to require from the officers or agents of the company, such information and explanations as the CSP may think necessary for the purpose of such certificate.

Attachment of Compliance Certificate with Board's Report:

Proviso to Sub-section (1) of section 383A of the Act requires that the Compliance Certificate shall be attached with the Board's report referred to in section 217. It is, therefore, necessary for the company to attach a company of the Compliance Certificate with the Board's report while forwarding the same to members and others under section 219 of the Act.

Further it would also be desirable for the Board to give full information and explanation in its report to the members under section 217 of the Act on every reservation, qualification or adverse remarks contained in the Compliance Certificate.

Laying of the Compliance Certificate at the Annual General Meeting:

Sub-rule(4) of rule 3 requires the Compliance Certificate to be laid by the company in its annual general meeting. As a good secretarial practice, the certificate should be read at the meeting and also made available to the members for inspection.

Penalty for Non-Compliance:

Where a company fails to comply with the requirement to be addressed to the members of the company, it would be in the fitness of things that the appointing authority is the members to whom this certificate is addressed. It is advisable that the CSP is appointed by the members in the annual general meeting of the company. Such appointment shall be from the conclusion of that annual general meeting until the conclusion of the next annual general meeting. It is also recommended that the first appointment of the CSP may be made by the Board of directors to hold office until the conclusion of the annual general meeting held after such appointment.

The Board may fill any casual vacancy in the office CSP to hold office until the conclusion of the next annual general meeting. However, if such a vacancy is caused by the resignation of CSP, it is advisable that the vacancy is filled up by the company in general meeting.

Disqualifications of Secretary in whole-time Practice:

With a view to ensure that CSP shows utmost integrity and independence of judgment in the performance of his duties, a person referred to in Sub-section(3) or Sub-section(4) of section 226 of the Act, should not be eligible for appointment or reappointment for giving Compliance Certificate to a company.

Accordingly, the following persons shall not be qualified for appointment as CSP of a company—

a) a body corporate;
b) an officer or employee of the company;
c) a person who is a partner, or who is in the employment, on an officer or employee of the company;

d) a person who is indebted to the company for an amount exceeding one thousand rupees, or who has given any guarantee or provided any security in connection with the indebtedness of any third person to the company for an amount exceeding one thousand rupees;
e) a person holding any security of that company which carries voting rights.

However, any securities held by such person is not qualified for appoint as CSP of a company for reasons stated above, then he is also disqualified for appointment as CSP of any other body corporate which is that company's subsidiary or holding company or a subsidiary of that company's holding company, or would be so disqualified if the body corporate where a company.

If a CSP becomes subject, after his appointment, to any of the disqualifications specified above, he shall be deemed to have vacated his office.

Communication to earlier Incumbent:

In view of the provisions of clauses (8) and (11) part I of the First Schedule to the Company Secretaries Act, 1980, it is recommended that whenever a new incumbent is assigned the compliance certification work, he should communicate his appointment to the earlier incumbent by registered post.

Methodology for Carrying out Verification for Certification:

It would be advisable that the CSP requests the company for access to various documents and books including the Memorandum and Articles of Association of the company, Annual Reports of the last two to three years, various statutory and other registers including the Minutes Books, copies of forms and returns filed with the ROC etc. which he considers essential for the purposes of laying down the certification programme.

CSP should verify all the available records. However, depending on the facts and circumstances he may obtain a letter of representation from the company in respect of matters where verification by CSP may not be practicable, for example matters like—

i) dis-qualification of directors
ii) show cause notices received
iii) persons and concerns in which directors are interested.

Certification with Qualification:

As specified in the Form, the qualification, reservation or adverse remarks, if any, may be stated by the CSP at the relevant places.

If the scope of work required to be performed, is restricted on account of limitations imposed by the client or on account of circumstantial limitations (like certain books or papers being in custody of another person or Government Authority) the certificate may be qualified as such.

CSP shall have due regard to the circulars and / or clarifications issued by the Department of Company Affairs from time to time. It is recommended that a specific reference of such circulars at the relevant places in the certificate may be made, wherever necessary.

Penalty for false Compliance Certificate:

Section 628 deals with penalty for false statements. According to this section, if in any return, report, certificate, balance sheet, prospectus, statement or other document, required by or for the purpose of any of the provisions of the Act, any person makes a statement-

(a) which is false in any material particular, knowing it to be false or
(b) which omits any material fact, knowing it to be material;

he shall, except as otherwise expressly provided in the Act, be punishable with imprisonment for a term which may extend to two years and shall also be liable to fine.

In view of this, a CSP will be attracting the penal provisions of section 628, for any false statement in any material particular or omission of any in any material particular or omission of any material fact in the Compliance Certificate. However, a person will be penalised under section 628 in case he

makes a statement, which is false in any material particular, knowing it to be false, or which omits any material fact knowing it to be material.

Professional responsibility:

While the newly inserted provision has opened up the much awaited significant area of practice for company secretaries, it equally casts onerous responsibility on them and poses a greater challenge whereby they have to justify fully the faith and confidence reposed by the Government and trade and industry and measure up to their expectations. Company Secretaries much take adequate care while issuing Compliance Certificate. It is based on this certificate that confidence of the company, Government and trade and industry will build-up vis-à-vis our profession. Any failure or lapse on the part of a CSP in issuing a Compliance Certificate may not only attract penalty for false statement under section 628 and disciplinary action for professional or other misconduct under the provisions of the Company Secretaries Act, 1980 but also make him liable for any injury caused to any person due to his negligence in issuing the Compliance Certificate. Therefore, it becomes imperative for the CSP that he exercises great care and caution while issuing the Compliance Certificate and also adheres to the highest standards of professional ethics and excellence in providing his services.

Fees for Compliance Certificate:

The scale of fees for compliance certification may be based on criteria, like paid-up share capital, number of shareholders and debenture holders, nature and standard of secretarial practices prevalent in the company, man-hours involved etc. however, the minimum fee for certification shall ordinary not be less than Rs.5,000 for a financial year.

Checklist:

Articles of Association:

Checklist for Secretarial Compliance with regard to Articles of Association.

(a) Check the extent of applicability of Table A of Schedule I to the Act.

(b) Check whether the articles were altered during the year. If so, check whether:

i) copy of the special resolution was filed with the Registrar in Form No.23;

ii) the change had been incorporated in all copies of the articles; and

iii) the alteration had the effect of converting a public company into a private company, if so check whether:

- approval of the Central Government was obtained; and
- a printed copy of the articles as altered was filed with the Registrar within one month of the date receipt of the order of approval.

Borrowing Powers:

(a) Check the Memorandum and Articles with respect to the powers of the company to borrow money and the charge the assets of the company.

(b) check if the power to issue debentures has been delegated to exercised at the meeting of the Board.

(c) check whether the power to borrow money, otherwise than on debentures, has been exercised at the meeting of the Board.

(d) if the power to borrow money otherwise than on debentures has been delegated to a committee of directors or managing director or manager or any other principal officer of the company, check that the delegation was made at the meeting of the Board and the resolution delegating the power specified the total amount outstanding, at any time, up to which the money may be borrowed by the delegate.

(e) where the total amounts borrowed (apart from temporary loans obtained form the company's bankers in the ordinary course of business) exceed the aggregate of the paid-up capital of the company and its free reserves, check that consent of the members in general members has been obtained.

Membership of a Company:

(a) As per Section 41of the Companies Act, the various modes by which a person can become a member of a Company are –

(i) by subscribing to the Memorandum of Association of the Company;

(ii) by agreeing to become a member;

(a) by making an application to the company for allotment of shares or

(b) by executing an instrument of transfer of shares as transferee or

(c) by consenting to the transfer of shares of a deceased member in his name or

(d) by acquiescence or estoppel;

and on him name being entered in the register of members.

Also every person holding equity shares of the Company and whose name is entered in as beneficial owner in the records of a depository shall be deemed to be a member of the Company.

(b) (i) One of the most important criterion of becoming a member of a Company is legal entity i.e. the member must be a legal person.

A partnership firm is not a legal person and as such it cannot in its own name become a member of a Company. However, its partners may become joint shareholders of a Company and their names may be entered in the register of member.

(ii) A Company (both Public and Private) can become a member of another Company. Since a company is legal person and is competent to enter into a contract in its own name, it can become a member of any other Company. However, the Company must be authorised by its Memorandum of Association to invest the shares of other Company otherwise it cannot become a member of any other company. A subsidiary Company cannot become a member of its holding Company. Also a Company can not become a

member of itself. Therefore a private limited Company can become a member of a Company subject to certain conditions.

(c) As per Section 42, a body corporate cannot be a member of a Company which is its holding Company and any allotment or transfer of shares in a Company to its subsidiary shall be void; except

  (i) where the subsidiary holds shares in the holding company in the capacity of a legal representative of a deceased shareholder, or
  (ii) where the subsidiary holds shares as trustee, or
  (iii) where the subsidiary held shares in the holding Company before it become its subsidiary. In this case the subsidiary can continue to hold the shares but, without right to vote at meetings of the holding Company.

Number and Appointment of Directors:

1. Check Whether the company has the minimum number of Directors;
2. in case the number fell below the minimum whether action has been taken to bring it to the minimum;
3. If it's a new company, check if the first directors were appointed in accordance with the articles;
4. check that the provisions of sections 255 and 256 have been duly complied with;
5. ensure that persons other than retiring directors who were candidates for directorship at the general meeting had complied with the provisions of Section 257.
6. if the number directors has been increased to more than 12,check whether approval of the Central Government has been obtained
7. if the board has appointed addition directors, check if the appointment was in accordance with the articles.

8. if the board has filled up casual vacancy among directors appointed in general meeting, check if the appointment was in accordance with the articles and was made at a meeting of the Board.
9. if the board has approved any alternate / additional director during the year, check that it was authorised to do so under section 313 and 260 respectively;
10. if any nominee directors have been appointed during the year, check whether the appointment is in consonance with the provisions of the articles of the company and the loan agreement. Also check whether the approval of the Government, under Section 259, if required, has been obtained.
11. check whether each of the directors had given consent to act as director within 30 days of his appointment and the consent was filed with the Registrar in Form No.29.
12. check with reference to Section 274 that none of the directors suffers from any of the disqualifications.

Appointment of Managerial Personnel:

I. In case of private company not being a subsidiary of a public company

- Check whether the appointment has been made in conformity with the provisions in the Articles of Association.

II. In case of other company

Check whether:

(a) the appointment was made in accordance with the provisions of Section 269 read with schedule XIII,

(b) the appointee has furnished a declaration or otherwise stated that he satisfies the conditions specified in Part I of Schedule XIII,

(c) if appointment had been made without the approval of the Central Government,

i. the appointment was in accordance with the conditions specified in Schedule XIII;

ii. return in Form No.25 C was filed with the Registrar within 90 days of the date of appointment; and

iii. the appointment had been approved by the members in general meeting.

(d) Where the appointment required the approval of the Central Government, application in Form No.25A seeking the approval of the Central Government was made within ninety days of the appointment and whether the approval of the Central Government has been received.

(e) The appointment was approved by the financial institutions, where ever required.

(f) Remuneration paid to Directors / Managing / Whole-time Directors is in accordance with the provisions of the Act and terms and conditions of approval.

Nomination:

With effect from the 31st October 1998, the Companies Act, 1956, permits a member to appoint a nominee who will be entitled to all the shares and benefits there under in the event of the members unfortunate death or other incapacity.

(i) The Nomination can be made by individuals only applying / holding shares / debentures on their own behalf singly or jointly upto two persons. Non-individuals including society, trust, body corporate, partnership firm, Karta or Hindu Undivided Family, holder of power of attorney cannot nominate. If the shares are held jointly all joint holder will sign the nomination form.

(ii) A minor can be nominated by a holder of shares / debentures / deposits and in the event the name and address of the Guardian shall be given by the holder.

(iii) The nominee shall not be a trust, society, body corporate, partnership firm, Karta of Hindu Undivided Family or a power of attorney holder. A non-resident Indian can be a nominee on repatriable basis.

(iv) Nomination stand rescinded upon transfer of share / debenture or repayment / renewal of deposits made.

(v) Transfer of share / debenture in favour of a nominee and repayment of amount of deposit to nominee shall be a valid discharge by a Company against the legal heir.

Rights of a Nominee under Sections 109A and 109B -

Right to Nomination:

(i) The rights of a nominee arise only on the death of the shareholder.

(ii) On the death of the shareholder, the nominee may either get himself registered as the holder or, make transfer of shares as the deceased shareholder could have made.

(iii) The nominee on becoming entitled to the shares by reason of death of the holder shall be entitled to the same dividends and other advantages to which he would be entitled if he were the registered shareholder, except for the right in respect of membership that can be exercised in relation to meetings of a Company.

Rights of the company under Sections 109A and 109B

(i) The company has the right to require the nominee to produce such evidence as specified by the Board.

(ii) The Company has the right to give notice to the nominee requiring him to elect either to be registered as a shareholder or to transfer the shares. If the nominee does not comply with the notice within 90 days, the Company has the right to withhold payment of all dividends, bonuses or other moneys payable in respect of the shares until the requirements are complied with.

Steps to be taken by nominee to register himself as shareholder:

Any person who becomes a nominee by virtue of Section 109A, has to do the following to register himself as a shareholder:

(a) Produce such evidence as may be required by the Company;

(b) Deliver or send to the Company a notice in writing signed by him stating that he elects to be registered as a shareholder of the Company;

(c) The written notice should be accompanied with the death certificate of the deceased shareholder.

(d) If the Board, at any time has issued a notice to the nominee requiring him to elect either to be registered himself as the shareholder or to transfer the shares, the nominee has to within 90 days of the notice inform the Company in writing, regarding his decision.

Transfer of Shares:

Transfer of Shares means the transfer of the ownership of the shares from one person to another subject only to the provisions of the Act and restrictions, if any, laid down on the Articles of the Company. An important characteristics of shares is their transferability and Section 82 of the Act empowers every shareholder to transfer his shares in the manner prescribed by the Act and as per the Articles of the Company. Transfer of shares is effected by removing the name of the existing shareholder from the register of member and by inserting the name of the new person in place of the removed one in the register of members.

If the instrument of transfer is found to be incomplete in any respect, the Company immediately returns it along with a covering letter stating the defect / deficiency (which is usually a letter having a standard format), to the person from whom it was received for making good the deficiency.

Transfer of shares in dematerialised form – Transfer of shares in the dematerialised form can be either inter-depository participants (Inter-DPS) or intra-depository participants (intra-DP). In both cases the transfer is effected when selling client submits a request to the Depository for transferring balances from its account to another account. After checking signature, identity etc. of the selling client, the selling clients (transferors) account will be debited and the buying clients (transferee's) account will be credited.

No stamp duty is payable on the transfer of shares in the dematerialised form.

Checklist for Audit of Transfer Deeds:

Before giving effect of any transfer of shares it is to be seen whether the transfer deed is properly filled or not. For assuring such correctness one has to prepare a list of the items which are to be checked and such a list of items is known on 'checklist'. A checklist for scrutinising a transfer deed should ensure:

(i) whether the instrument is given in prescribed Form 7B;

(ii) whether the instrument is properly dated and whether the date of execution of instrument falls on the said date or subsequently.

(iii) Whether the instrument has been presented to the Company within the validity period.

(iv) Whether the instrument has been lodged with the Company with the date extended, if any by ROC.

(v) Whether the signature of the transferor agrees with the specimen signature registered with the Company.

(vi) When the signature of the transferor on the transfer deed does not tally with the specimen recorded with the company, the documents have to be returned for obtaining fresh signature of the transferor.

(vii) Whether the instrument has been duly stamped as per provisions of the Indian Stamp Act, 1899 as amended from time to time, at present the stamp duty on transfer deed of shares is @ of fifty paise for every hundred rupees of consideration.

(viii) Whether the transferee has signed the transfer deed and has given his specimen signature.

(ix) Whether the share transfer deed is accompanied with share certificate or letter of allotment.

(x) whether the distinctive number of shares as per the share certificate are the same as mentioned in the transfer deed;

(xi) whether the share proposed to be transferred stand in the name of the transferor in the register of members.

(xii) In case when the transfer deed has been executed by an Attorney, whether the power of attorney has been seen and found in order.

(xiii) If the transfer is proposed in favour of a minor whether the Articles permit such transfer.

(xiv) In case when either / the transferor or the transferee is a NRI whether permission of the RBI has been obtained.

(xv) When transfer is in favour of minor / karta of HUF/ Partnership firm/ trust whether the deed is executed by the person authorised to do so.

(xvi) Where the transfer is in favour of a Company, whether the memorandum has been checked for the power to invest in and whether authority to sign the instrument has been furnished .

(xvii) Whether the instrument is complete in all other respect i.e.

(a) Properly witnessed and

(b) Occupation and address of the transferee duly given

(xviii) Whether transferees Folio No. old / new is given

(xix) In case the transferee is a blank whether general power of Attorney is enclosed.

(xx) Whether the shares are attached by any Government authority and if so, whether the deed has been signed by such authority.

General Meeting

(a) Statutory Meeting:

Ensure that:

i) notice of meeting and statutory report in Form No.22 duly certified were sent to the members and Registrar of Companies; and

ii) other requirements of general meeting, e.g. quorum, notice, preparation and signing of minutes, etc., were complied with.

(b) Annual General Meeting:

Ensure that:

1. the first Annual General Meeting is held with 18 months from the date of incorporation of the company;
2. subsequent Annual General Meetings are held in each year and the time between two successive meetings has not been more than 15 months;
3. the provisions Section 210 have been complied with;
4. other requirements e.g., notice, quorum, chairman, proxy, preparation and signing of minutes etc., were complied with;
5. annual return has been filed within 60 days from the date of Annual General Meeting of the AGM has not been held, within 60 days from the latest day it ought to have been held; and
6. meetings have been called during business hours on a day not being a public holiday and held at the registered office of the company or at anyplace in the same city, town or village.

(c) Extraordinary General Meeting:

Check Whether:

1. the requisition set out the matters for consideration and has been signed by members holding not less than 1/10th of the paid-up capital with voting rights or 1/10th of the total voting power, as the case may be;
2. the Board, within 21 days of deposit of a valid requisition, proceeded to call a meeting on a day within 45 days for such date of deposit of requisition;
3. other requirements e.g., quorum, proxy, maintenance of minutes of a general meeting were complied with; and
4. in case the meeting had been called by requisitionists, reasonable expenses incurred by them had been reimbursed by the company and this sum had been recovered for the defaulting directors.

Declaration of Dividends:

Ensure that:

1. dividends are declared out of profits after providing for depreciation according to the provisions of Section 205(2);
2. specified minimum amount is transferred to reserves according to the companies (Transfer of Profits to Reserves) Rules, 1975;
3. board resolution recommending dividends has been passed;
4. the Board has authorised the opening of separate Bank Account for payment of dividend;
5. register of members was closed as per provisions of Section 154;
6. dividend was declared at the Annual General Meeting;
7. dividend warrants were printed, signed and dispatched to the registered shareholders within 30 days of declaration;
8. tax deducted at source is deposited within seven days of the issue of dividend warrants;
9. permission of Reserve Bank of India was obtained before dividend was remitted to foreigners / non-resident Indians;
10. stock exchange was duly intimated, in case of listed company;
11. approval of the financial institution is taken if the company has taken loans from financial institution and the rate of dividend exceeds the permitted rate;
12. unpaid / unclaimed dividend is transferred to Investor Education and Protection Fund

FORM

Compliance Certificate

[See Rule 3]

To

The Members,

……………………………… (Name of the Company)

I / We have examined the registers, records, books and papers of ………………………… Limited (the Company) as required to be maintained under the Companies Act, 1956 (the Act) and the rules made there under and also the provisions contained in the Memorandum and Articles of Association of the comp[any for the financial year ended on 31st March, 20 …………… In my/ our opinion and to the best of my / our information and according to the examination carried out by me / us and explanations furnished to me / us by the company, its officers and agents, I/We certify that in respect of the aforesaid financial year:

1. the company has kept and maintained all registers as stated in Annexure 'A' to this certificate as per the provisions and the rules made there under and all entries therein have been daily recorded.
2. the company has duly filed the forms and returns as stated in Annexure 'B' to this certificate with the Registrar of Companies, Regional Director, Central Government, Company Law Board or other authorities within the time prescribed under the Act and the rules made there under.
3. the company being private limited company has the minimum prescribed paid-up-capital ad its maximum number of members during the said financial year was ……………………… excluding in present and past employees and the company during the year under scrutiny.

(i) has not invited public to subscribe for its shares or debentures;

(ii)has not invited or accepted and deposits from persons other than its members directors or their relatives.

4. the Board of Directors duly met …………… times ……………… (dates) in respect of which meetings proper notices were given and the proceedings were properly recorded and signed including the circular resolutions passed in the Minutes Book maintained for the purpose.

5. the company closed its Register of Members, and / or debenture holders from ……………………… to ………………… and necessary compliance of section 154 of the Act has been made.

6. the Annual General Meeting for the financial year ended on ……………………… was held on …………………. after giving due notice to the members of the company and the resolutions passed thereat were duly recorded in Minutes Book maintained for the purpose.

7. ……………………… Extraordinary meeting(s) was / were held during the financial year after giving due notice to the members of the company and the resolutions passed thereat were duly recorded in the Minutes Book maintained for the purpose.

8. the company has advanced loan amounting to Rs………………. to its directors and / or persons or firms or companies referred in the section 295 of the Act after complying with the provisions of the Act.

9. the company has duly complied with the provisions of section 297 of the Act is respect of contracts specified in that section.

10. the company has made necessary entries in the register maintained under section 301 of the Act.

11. the company has obtained necessary approval from the Board of Directors, members and previous approval of the Central Government pursuant to section 314 of the Act wherever applicable.

12. the Board of Directors or duly constituted Committee of Directors has approved the issue of duplicate share certificates.

13. the company has:

(i) delivered all the certificates on allotment of securities and on lodgement thereof for transfer / transmission or any other purpose in accordance with the provisions of the Act;

(ii) deposited the amount of dividend declared including interim dividend in a separate bank account on .... which is within five days from the date of declaration of such dividend.

(i) paid / posted warrants for dividends to all the members within a period of 30 days from the date of declaration and the all unclaimed / unpaid dividend has been transferred to Unpaid Dividend Account of the Company with .... Bank on ....

(ii) transferred the amounts in unpaid dividend account, application money due for refund, matured deposits, matured debentures and the interest accrued thereon which have remained unclaimed or unpaid for a period of seven years to Investors Education and Protection Fund.

(iii) Duly complied with the requirements of section 217 of the Act.

14. the board of Directors of the company is duly constituted and the appointment of directors additional directors, alternate directors and directors to fill casual vacancies have been duly made.

15. the appointment of Managing Director / Whole-time Director / Manager has been made in the compliance with the provisions of section 269 read with Schedule XIII to the Act and approval of the Central Government has been obtained in respect of appointment of .... not being in terms of Schedule XIII.

16. the appointment of sole-selling agents was made in compliance of the provisions of the Act.

17. the company has obtained all necessary approvals of the Central Government, Company Law Board, Regional Director, Registrar or such other authorities as may be prescribed under the various provisions of the Act as detailed below:

18. the directors have disclosed their interest in other firms / companies to the Board of Directors pursuant to the provisions of the Act and the rules made there under.

19. the company has issued .... shares / debentures / other securities during the financial year and complied with the provisions of the Act.

20. the company has bought back …………………… shares / debentures / other securities during the financial year ending ……………… after complying with the provisions of the Act.

21. the company wherever necessary has kept in abeyance right to dividend, rights shares and bonus shares pending registration of transfer of shares in compliance with the provisions of the Act.

22. the company where necessary has kept in abeyance rights to dividend, rights shares and bonus shares pending registration of transfer of shares incompliance with the provisions of the Act.

23. the company has complied with the provisions of sections 58A 58AA read with Companies (Acceptance of Deposit) Rules, 1975 / the applicable directors issued by the Reserve Bank of India / any other authority in respect of deposits accepted including unsecured loans taken, amounting to Rs………………… raised by the company during the year and the company has filed the copy of Advertisement / Statement in lieu of Advertisement / necessary particulars as required with the Registrar of Companies …………… On ………………… The company has also filed return of deposit with the Registrar of Companies / Reserve Bank of India / other authorities.

24. the amount borrowed by the Company from directors, members, public, financial institutions, bank and other during the financial year ending – is / are within the borrowing limits of the company and that necessary resolutions as per section 293(1)(d) of the Act have been passed in duly convened annual / extraordinary general meeting.

25. the company has made loans and investments, or given guarantee or provided securities to other bodies corporate in compliance with the provisions of the Act and has made necessary entries in the register kept for the purpose.

26. the company has altered the provisions of the memorandum with respect to situation of the company's registered office from one state to another during the year under scrutiny after complying with the provisions of the Act.

27. the company has altered the provisions of the memorandum with respect to the objects of the company during the year under scrutiny and complied with provisions of the Act.

28. the company has altered the provisions of the memorandum with respect to name of the company during the year under scrutiny and complied with the provisions of the Act.

29. the company has altered the provisions of the memorandum with respect to share capital of the company during the year under scrutiny and compiled with the provisions of the Act.

30. the company has altered its articles of association after obtaining approval of members in the general meeting held on .... and the amendments to the articles of association have been duly registered with the Registrar of Companies.

31. a list of prosecution initiated against or show-cause notices received by the company for alleged offences under the Act and also the fines and penalties or any other punishment imposed on the company in such cases is attached.

32. the company has received Rs. .... as security from its employees during the year under certification and the same has been deposited as per provisions of section 417(1) of the Act.

33. the company has deposited both employee's and employer's contribution to Provident Fund with prescribed authorities pursuant to section 418 of the Act.

Signature
Name of the Company Secretary
C.P.No.

Place :
Date :

Annexure A

Registers as maintained by the Company

1. …………………………… u/s……………………………
2. …………………………… u/s……………………………
3. …………………………… u/s……………………………

Annexure B

Forms and Returns as filed by the Company with the Registrar of Companies, Regional Director, Central Government or other authorities during the financial year ending on 31st March, 20……..

1. Form No. ……………………… Filed u/s ……………………for
2. Form No. ……………………… Filed u/s ……………………for
3. Form No. ……………………… Filed u/s ……………………for

* * *

Review Questions:

1. What is meant by compliance certificate ?
2. Explain the provisions of section 383a (1) of the companies act, 1956 regarding compliance certificate.?
3. Who can issue compliance certificate? State the contents of compliance certificate rules, 2001?
4. Explain the need and scope of secretarial compliance report. [C.S. Dec. 1997]
5. Prepare a check list for secretarial compliance with regard to
   a. Appointment of Auditor and
   b. Appointment of whole-time director, managing director and manager. [C.S. Dec. 2000]

6. Give a check list for verifying the compliance with the various covenants of a loan agreement with a financial institution in respect of the following:
   a. Security
   b. Utilisation of money advanced
   c. Leasing and trading activities. [C.S. June 2000]

7. Prepare a check list for secretarial compliance with regard to
   a. Board meeting and
   b. Payments made under the Payment of Bonus Act, 1965. [C.S. Dec. 1999]

8. Prepare a check list for secretarial compliance in respect of the following:
   a. Registration / Modification of a charge.
   b. Declaration of dividend. [C.S. June 1999]

9. Prepare a check list for secretarial compliance of the following:
   a. Borrowing powers of the company.
   b. Invitation, acceptance and renewal of deposits under the Companies (Acceptance of Deposits) Rules 1975. [C.S. Dec. 1998]

10. Prepare a check list for secretarial compliance in respect of the following:
    a. Registration / modification of charges
    b. Listing agreements under the Securities Contracts (Regulation) Act, 1956.

11. Prepare a checklist for secretarial compliance with regard to articles of association. [C.S. Dec. 1997]

12. State the check list for
    a. Further issue of capital
    b. General meetings and
    c. Declaration of dividends.

LESSON 6
MANAGEMENT AUDIT

Objective:

After reading this lesson, the students should be able to under stand the features of Management Audit, Objectives and Scope of Management Audit, Polices and Systems and Procedures, Organisational needs for Management Audit and distinction between Management Audit and Financial Audit.

Learning Activities:

Reading of

i. Secretarial, Securities and Management audit
by Dr.V.Balachandran & K.S.Ravichandran
Bharath Law Book House, New Delhi

ii. Cost and Management Audit
by A.R.Ramanathan
Tata McGraw Hill, New Delhi

iii. Cost and Management Audit
by Vashist & Saxena
Sultan Chand & Sons, New Delhi

iv. ICSI Study Materials

- Definition:
- Features of Management Audit
- Objectives of Management Audit:
- Policies, Systems and Procedures:
  - Enquiry:
  - Examination:
  - Confirmation:
  - Observation of Pertinent Activities and Conditions:
  - Correlation of Information
- Efficiency Audit
- Special Audit:
- Operational Audit:
- Propriety Audit:

- Organisational Needs of Management
- Distinction between Management Audit and Financial Aduit:

Meaning:

Management audit is a systematic fact finding approach that examines, appraises and reports on the understanding and effectiveness of the organisations objectives, policies, standards, structure, procedures and controls to identify friction, waste, etc. and to identify areas for improvement.

Features of Management Audit:

Management audit is a systematic, comprehensive, critical appraisal of the organisation structure. Management practices and methods conducted normally by external independent person. Its primary objective is to motivate management to take action which will lead to increased efficiency and profitability of the organisation. It covers all the functional areas of management i.e. planning, organising, coordinating, controlling etc. It is a systematic and dispassionate study analysis and appraisal of the management's overall performance.

Objectives:

1. To identify the overall objectives of a business enterprise and to see that these objectives are being fulfilled in actual practice.
2. To ensure optimum utilisation of human resources and available physical facilities.
3. To see that management is efficient at levels of operations.
4. To suggest improved and better methods of managerial operations.
5. To point out weak spots in the organisation structure and in internal control system and suggesting possible improvements.

Management auditing is a vital exercise and embraces conducting the audit for the management as also auditing of the management. Management has to evolve governing rules and regulations, and for carrying out the activities it has to plan, direct and control. Thus management process and functions.

Management auditor may examine, review and appraise the various policies and actions of the management on the basis of certain objective standards to assist all levels of management in the effective discharge of their responsibilities. As it involves review of the management. The auditor has to review every matter under audit not only from the true and fair angle but also from the management angle. Management is concerned with not only an efficient operation of the business but also with its effectiveness in relation to management objectives. Since management audit is relatively a new area for audit, its dimensions are varied from the finance function to technical or scientific activities, the management objectives. Since management audit is relatively a new area for audit, it dimensions are varied from the finance function to technical or scientific activities, the management auditor ahs to extend his professional knowledge either by acquiring the required know-how or supplement by constituting an audit team composed of experts from different areas. Management audit, if properly undertaken, is an excellent tool of management control in may situations. This concept offers entirely new dimension to the audit functions and has great potential.

Management audit is comprehensive and constructive examination of an organisational structure or its components, such as a division or a department, its plans and policies, its financial controls, its methods of operation and its use of human and physical facilities. It is a form of appraisal and assessment of managerial performance by means of an independent and dispassionate examination as to how far the plans drawn up have been complied with, the standards set-up have been attained and the policies have been pursued. Its primary objective is to motivate management to take action which will lead to increased efficiency and profitability of the organisation. It is seen that management audit is concerned with appraising management's accomplishment of organisational objectives, the management functioning of planning, organising, directing and controlling and the adequacy of management's decisions and actions towards its stated objectives and policies. Thus, the accent is on evaluating the management policies, its performance and procedures.

Policies, Systems and Procedures:

1. Who is responsible for designing the system? If there is a separate department, is it adequately manned with qualified people?
2. Are there proper descriptions, flows charts and manuals showing various systems?
3. Are the systems related to the changing technology and environment of the business? Is there a periodic review of the system to modify them in this context?
4. Is there a periodic review of the costs and the related benefits of a particular system?
5. What are the various forms in use? Are they designed to give proper information with minimum effort?
6. What are the steps taken to reduce paper work?
7. While recommending a new system, are all the relevant factors taken into account?
8. There are new systems properly explained to various people before they are put into operation?
9. Is the routing of various forms are statements periodically reviewed keeping in view the need for information at the various levels and possibility of delay?
10. Are the filing and storing procedures for various documents properly laid down?

The management auditor can use the following techniques to conduct the audit:

1. **Enquiry**:

Most of the evidence required is collected by asking relevant questions and obtaining satisfactory answers.

2. **Examination**:

In many cases examination of documents and records becomes necessary in case the enquiry process yields certain information which needs collaboration or which suffers from internal contradictions.

3. **Confirmation**:

A management auditor may also obtain written or oral statements from various persons in order to confirm the information obtained by him.

4. **Observation of Pertinent Activities and Conditions**:

In may cases the management auditor may have to rely upon his own observation of pertinent activities and conditions in the organisation.

5. **Correlation of Information**

The information collected through the various techniques has to be correlated so that proper conclusions can be arrived at.

The decision making process pervades the entire managerial function. An appraisal of the effectiveness of management decisions involves minute study of various decisions, the extent to which the desired results have been achieved and identifying the deficiencies and shortcomings so that corrective and preventive actions be recommended to the management. The following steps are involved in appraising the effectiveness of management decisions;

(1) examining the nature, type, operations and objectives of business

(2) examining the corporate policy, planning criteria and its adequacy.

(3) Checking the delegation of powers to functional heads and its adequacy.

(4) Examining the data used for analysis, evaluation and decision making.

(5) Compilation of the data required for analysis and evaluation. Questionnaires, interviews, examination of available records, personal observation comparison, etc., may be used for this purpose.

(6) Analysing the regularity of review of variances and corrective actions taken

(7) Checking how many decisions are for crisis, losses, if any, and the causes for the same and precautions taken.

(8) Examining the adequacy and awareness of management regarding market forecasts.

(9) examining the team decisions and functional budgets. The skills required for the team specialist are to be examined.

(10) Analysing the validity of historical information which form the basis of budgets.

(11) Examining the adherence of decisions to the objectives laid down and the constraints to decision making because of laws, statues, etc.

(12) Ensuring the adequacy and timeliness of demarcation of authority for decision making vis-à-vis the requirements of the day.

(13) Examining the extent of co-ordination among executives and the degree of harmony among them. The quality of each individual must be assessed and the value of his contribution to be evaluated, bearing in mind the needs of the company.

(14) examining the areas of conflict of interest among team decision makers.

Decision making is similar to problem solving. It calls or identifying and defining the problems, defining the expectations or objectives of the decision, developing alternatives and evaluating them, selecting the best possible choice and then taking decision. The main aspect of appraisal of management decisions is to validate the monitoring systems in terms of adequacy, efficiency and effectiveness.

The terms 'management audit", 'operational audit' and the modern concept of 'internal audit' often convey more or less the same meaning. There is no clear-cut demarcation of the areas / audit activities. In an audit assignment to review operations and performance, it is difficult to say which portion of the audit programme relates to internal audit, to operational audit and to management audit. There is a considerable overlapping in the scope and content of the audits.

British Institute of Management has defined: "Management audit is a systematic, comprehensive critical appraisal of the organisation, structure, management practices and methods conducted normally by external independent persons. Its primary objective is to motivate management to take action which will lead to increased efficiency and profitability of the organisation".

The institute of Internal Auditors, USA defines-"Internal auditing is an independent appraisal function established within an organisation to examine and evaluate its activities as a service to the organisation. The objective of internal auditing is to assist members of the organisation in the effective discharge of their responsibilities, counsel and information concerning the activities reviewed". This implies that an internal auditor has to go beyond the books of accounts and related records and appraise the quality of various organisational activities. The task involves a review of operations.

While internal audit is being basically conducted for control of various operations, control measures etc. for and behalf of the management of the company as an aid to management, management audit covers not only these aspects but also at times to know the efficiency of the management functions itself and can even be a review of activities of the management itself.

Operational audit has been defined by the Federal Financial Officers' Institute, Canada as follows:

> "A systematic independent appraisal activity within an organisation for a review of the entire departmental operations as a service to management. The overall objective of operational auditing is to assist all levels of management in the effective discharge of their responsibilities by furnishing them with objective analysis, appraisals, recommendations and pertinent comments concerning the activities reviewed".

Some authors have attempted to distinguish between 'operational audit' and 'management audit'. Accordingly, operational audit is confined to various activities and operations in the functional areas. Whereas management audit deals with all aspects of the management process. It is an audit to examine, review and appraise the various policies and actions of the management on the basis of certain standards. It goes beyond the conventional financial audit which

involves a scrutiny of financial transactions and the books of account. It is a comprehensive and critical review of all aspects of management process.

Types of Audit:

i) Efficiency Audit

Efficiency audit presupposes certain levels of efficiency at which the operations are being carried on. It establishes a relationship between input and output. It measures the efficiency with which the resources employed are being used. Efficiency audit is directed towards the assessment whether or not corporate plans have been economically and efficiently executed. Therefore, it deals with the functional / operational areas of the organisation to find out whether resources of the organisation both economic and physical are being utilised in the most effective and efficient manner in order to attain the objectives of the organisation. It consists of studying the plans or the organisation into the reason for variances, to take corrective action. Efficiency audit ensures that the flow of resources into the most remunerative channels, i.e. every rupee invested in investment between the different functions and aspects designed to give optimum results. The ultimate purpose of efficiency audit is to see whether the management control system has been functioning properly in its functional or operational areas. Broadly speaking the objects and aims of efficiency audit can be summarised to see the following:

(1) Whether the optimum return on capital has been achieved.

(2) Whether there are problems to achieve the desired goals and objectives.

(3) Whether there is utilised or under utilised capacity or resources.

(4) Whether man-power is properly harnessed and developed.

(5) Whether areas of uncertainty in business are reduced to minimum.

ii) Special Audit:

Section 233A of the Companies Act, 1956 empowers the Central Government to direct special audit of accounts of the company for a specified period , if in its opinion any of the following circumstances exist:

i. that the affairs of the company are not being managed in accordance with the sound business principles or prudent commercial practices;

ii. that the company is being managed in a manner likely to cause serious injury or damage to the interest of the trade, industry or business to which it pertains;

iii. that the financial position of the company is such as to endanger its solvency.

The Central Government can order a special audit of the accounts of the company if in its opinion any of the three circumstances mentioned above exists, without giving an opportunity of being heard to the management of the company. The Central Government may appoint for this purpose of the company's auditors or any other Chartered Accountant to conduct the special audit. The posers of duties of the special auditor of the company would be similar to that of the company's auditor. The company has to pay the remuneration for special audit and other related expenses as determined by the Central Government. The special auditor submits his report to the Central Government instead of the members of the company.

The report of the special auditor shall, as far as any be, include all the matters required to be included in an auditors report under section 227 and, if the Central Government so directs, shall also include a statement of any other matter which may be referred to him by the Government. The Central Government may take action on the basis of report submitted to it. If no, action is taken on this report within four months of its receipt, the Central Government has to send to the company either a copy of or relevant extracts from the report with its comments, to be circulated among the members or to be read out to them at the next general meeting.

iii) **Operational Audit**:

Operational audit refers to a systematic independent appraisal of activity within an organisation for a review of the entire departmental operations as a service to management. The overall objective of operational auditing is to assist all levels of management in the effective discharge of their responsibilities by

furnishing them with objective analyses, appraisals, recommendations and pertinent comments concerning the activities reviewed.

Operational audit is an impartial service to operational management which gives assurance when appropriate the operational objectives are valid; that operational control information is reliable, and that operational activities are effective and efficient. It is also an agent for change by identifying and improving operational effectiveness, efficiency or economy. Operational audit is concerned with the pursuit of economy, efficiency and effectiveness throughout all operations. Essentially, operational auditing is a more comprehensive activity designed to analyse organisation structure, internal systems, work flow, and managerial performance. In short, an operational audit is intended to provide a comparison and evaluation of the achievement of organisation towards its goal and objectives. While internal auditing is confined of examinations of financial and accounting matters, operational auditing is more concerned with overall goal achievement, effectiveness, of operating procedures and internal control, performance of individual mangers, and other non-official aspects of the operation of an organisation with operational expertise.

The operational audit is more of a technical analysis for appraisal and review rather than a financial cum accounting analysis under financial audit, the audit functions and objectives reach beyond the financial control aspect with the operating areas of the business such as production, purchase, quality control, storage, transportation, marketing, personnel, research, financial services etc. it is to point out that any lacunae audit the operations of any of its activities whether major or support. In short, operational audit aims at improving future business operations by concerning the auditor with all aspects of management.

iv) **Propriety Audit**:

Propriety audit may envisage as the audit concerning the decisions of executives, with an emphasis on public interest, financial discipline, basically to get audit satisfaction that such decisions are within the framework of sanction, authority, rules and procedures and law made by a competent body and to advice the executives either in preventing or reducing the losses and increasing productivity, improving performance by timely reporting. It refers to an audit whether the transactions are in public interest and whether they meet the

standards of conduct. Propriety audit ensures whether the transactions have been effected in conformity with established rules, principles and established standards.

Propriety audit is the verification of transaction of an organisation to ascertain that have been properly recorded in the books and that three has been no misuse of assets and wastage of funds. While undertaking a property audit, the auditor does not merely evaluate the evidence supporting a transaction. He examines the regularity, prudence and impact of various actions and decisions of the authorities and ascertains whether the operations are carried on with wisdom, faithfulness and economy and whether the concern is yielding expected results. While carrying out propriety audit the author should analyse the following facts:

i) whether the assets have been properly used and safeguarded against misuse.

ii) Whether the business funds have been properly used.

iii) Whether proper recording has been done in the appropriate books of account.

iv) Whether the actions are in accordance with commonly accepted standards of conduct and financial propriety.

v) That the management has functioned with ordinary prudence and actions are not opposed to public interest.

vi) That the actions are prima facie not more than what the occasion demands.

vii) That the authority has not been exercised by any person for his personal advantage but for the benefit of the business or public.

This system of examination of accounts is mainly adopted in the sphere of government departments and government concerns as public funds are utilised and invested therein. thus the audit conducted by the Comptroller and Auditor General of India is primarily based on the principle of propriety. As per section 227(1A) of the Companies Act, it is now obligatory on the part of the statutory auditor of a company to enquire into the propriety aspect of the transaction. I here emphasis is basically on the propriety aspect or appropriateness of the transactions and various actions / inactions of the management.

Organisational Needs for Management Audit:

1. Does the company have a defined organisational structure. Any formal organisation chart drawn?
2. Are the principles of formal organisation being followed?
3. What is the span of supervision?
4. Is there a regular system of motivation?
5. Does the work distribution take into account the modern theories of organisation?
6. Is there any informal organisation?
7. What are the various levels in the organisational hierarchy? Are the lines of authority and areas of responsibility clear?
8. What is the nature of superior subordinate relationship in general? Are the authority pattern fraternal in nature?
9. Does there also exist an informal organisation?
10. Is there adequate provision for executive development programmes?

Distinction between Management Audit and Financial Audit:

S.No.	Management Audit	Financial Audit
1.	There is no limitation as to the period to be covered. It is discretionary and not statutory.	It covers the business transactions of the past financial year. It is statutory.
2.	It is concerned with review of the past performance to ascertain whether it is in tune with the objectives, policies and procedures of the enterprise.	It is almost exclusive concerned with financial aspects of business transactions of the year under Audit.

3.	The management auditor reports on the performance of the management during a particular period and suggest ways to remedy the deficiencies, including the modification of objectives, policies etc.,	The auditor reviews the past financial records to report his opinion on the truth and fairness of the representatives made in the financial statements viz., the Balance Sheet as at the end of a prescribed period and the Profit and Loss Account for the said period. Examination of the performance of the management is beyond its scope.
4.	The auditor reports to the management	The Auditor reports to the owners i.e. shareholders.

* * *

Review Questions

1. What is meant by Management Audit? State its objectives.
2. Explain the nature and scope of Management Audit.
3. State the points to be considered before taking up Management Audit.
4. How will you conduct Management Audit?
5. Explain the various techniques for assessing the effectiveness of Management.
6. Distinguish between Management Audit and Financial Audit.
7. How will you conduct Operational Audit?
8. Differentiate Operational Audit from Internal Audit.
9. Write a note on Efficiency Audit?
10. What is 'management information system'? What are its purposes, characteristics and types?

[C.S. Dec.2000]

11. Write a note on the "special audit" [C.S. June2000]

12. Discuss the techniques for conducting management audit.

[C.S. Dec.1998]

13. (a)What is 'propriety audit' ? Mention some of the reporting requirements touching upon propriety aspects that may be included in the statutory auditor's report.

(b) the companies registered under the Companies Act, 1956 are subject to special audit. In this context, answer the following:

(i) Who can order the special audit ?

i. Who can be appointed as a special auditor?
ii. How is the special audit to be conducted and what is the limitation on the powers and duties of a special audit?
iii. To whom the special auditor shall make his report and who shall pay the fees of the special auditor?
iv. How is the special auditor's report dealt with?

[C.S. June 2000]

14. (a) Management audit is an audit of management policies their adequacy for proper performance and procedure adopted for further implementation of management policies." Explain.

(b) What is an efficiency audit? What factors increase, the efficiency of various input factors in general and human resources in particular ?

[C.S. June 1998]

LESSON 7

COST AUDIT

Objective:

After reading this lesson, the students should be able to under stand the meaning of cost audit, Objectives, Scope, Functions, Advantages of the Cost Audit, Types of Cost Audit, Statutory Cost Audit Report.

Learning Activities:

Reading of

i. Secretarial, Securities and Management audit
by Dr.V.Balachandran & K.S.Ravichandran
Bharath Law Book House, New Delhi

ii. Cost and Management Audit
by A.R.Ramanathan
Tata McGraw Hill, New Delhi

iii. Cost and Management Audit
by Vashist & Saxena
Sultan Chand & Sons, New Delhi

iv. ICSI Study Materials

After reading this lesson the students should be able to under stand the significance of Cost Audit, recognitions secured for the practising company secretaries and the various areas of practice:

- Definition
- Objectives
- Scope:
- Functions:
- Advantages of the Cost Audit:
- Types of Cost Audit:
- Statutory Cost Audit:
- What Constitutes Cost Accounting Records:
- Verification of Stores:
- Cost Audit Report.

Definition:

The terminology of Cost and Management Accountancy issued by the Chartered Institute of Management Accounts, London defines Cost Audit as *"the verification of cost records and accounts and a check on adherence to the prescribed cost accounting procedures and their continuing relevance".*

Cost audit is defined as "*the verification of the correctness of the cost accounts and adherence to the cost accounting principles, plans and procedures*".

Objectives:

1. to verify that the cost accounts have been properly maintained and compiled according to the cost accounting system.
2. to verify that the cost accounts have been periodically reconciled with the financial accounts so as to ensure the accuracy of cost accounts.
3. to ensure that the company is making optimum use of resources available in the form of men materials and machines.
4. to ensure that the cost accounts are correct to detect all errors and frauds to make inter-firm comparisons and suggest management for improving the performance.
5. to provide reliable audited cost data where escalation clauses are in operation in respect of certain contracts.

Scope, Functions and Advantages of the Cost Audit:

<u>**Scope**</u>:

Cost audit involves:

(i) the verification of the record of cost accounts like the accuracy of the cost accountants, costing techniques and cost reports;

(ii) Scrutinising these records to make sure that they adhere to the cost accounting principles and objectives.

Functions:

Cost audit function concentrates upon the following:

(i) Cost accounting system, the financial position and process of manufacture;

(ii) Variations in cost per unit of output; cost consumption of various items of input; realisation including export sales;

(iii) Quantities of production and sales; sales realisation including export sales;

(iv) Abnormal and non-recurring costs;

(v) Efficiency or performance adequacy of controls.

Advantages of Cost Audit:

Cost audit is immensely advantageous to the management society, shareholders of the company and the government.

(i) To the management

(a) Management will be provided with reliable data for its day-to-day operation like price fixing, control, decision making, etc.

(b) A close and continuous vigil on all wastages will be maintained through an adequate and proper system of reporting to the management.

(c) Cost audit helps to bring the inefficiencies in the working of the company to light and thereby assists management in taking corrective action.

(d) Cost audit helps in fixing responsibilities to individual managers which in turn facilitates management by exception.

(e) Control tools like standard costing and budgetary control will be facilitated.

(f) Closing stock and work-in-progress valuation can be established with great accuracy.

(g) It is useful in the detection of errors and fraud.

(ii) To the society

(a) Consumers are protected for exploitation: Normally cost audit is conducted for the purpose of granting subsidies, protection and fixing prices. These prices are based on reliable and correct cost data and hence the consumers are saved from any exploitation.

(b) Standard of living is maintained – Price increase is allowed only after proper justification is made for increase in cost of production and thus consumers can maintain their standard of living.

(iv) To shareholders

The shareholders are assured of a fair return on their investment-with the help of cost audit shareholders can satisfy themselves about the valuation of closing stock and work-in-progress. Further it also makes sure that proper records are kept regarding purchases and utilisation of materials. They can also ensure that sales are into made below cost in normal circumstances.

(iv) To Government:

(a) Cost audit helps the government in fixing prices of essential commodities. It acts as a check on undue profiteering.

(b) It helps to identify the inefficient units.

(c) In respect of cost plus contract it helps the government in fixing a reasonable price of contract.

(d) Cost audit facilitates amicable settlement of trade disputes.

(e) It helps in bringing a healthy competition amongst units in an industry and this in turn imposes an automatic check on inflation.

Types of Cost Audit:

Primarily cost audit is carried out at the instance of the management for certain advantages. Further there are certain other circumstances also which necessitate audit of cost accountants. The following are some of the types of cost audit:

(i) Cost Audit on behalf of the Management:

The primary motive behind this audit is to ensure that the cost data placed before the management are thoroughly examined and dependable and that these are prepared in such way so as to serve the needs of the management in arriving at vital decisions. The following are some of the objectives of this type of cost audit:

(1) To establish the accuracy / correctness of cost data. Example: Cost of materials utilised, allocation of wages into direct and indirect;

(2) To ensure that cost accounting objectives are achieved through appropriate collection, allocation and compilation of cost data;

(3) To ascertain abnormal losses and gains together with their relevant causes;

(4) To determine the unit cost of production;

(5) To establish proper overhead rates for absorption of overheads by units produced;

(6) To fix contract price/selling price;

(7) To improve the quality of cost accounting system by obtaining comments and recommendations of their cost auditor;

(8) To use cost data for cost control purposes;

(9) To develop cost accounting records from period to period, year to year basis for comparison of performance.

(ii) Cost Audit on behalf of a Customer:

This type of cost audit is normally adhered to in respect of cost plus contracts. Normally, the contract or the buyer insists for a cost audit to have accurate estimation of cost.

(iii) Cost Audit on behalf of Government:

Before granting subsidies, protection, fixing selling price etc. the government may like to conduct cost audit to determine the cost of manufacture of the product and thereby satisfy itself about the genuiness of the need for subsidies, protection, level of selling prices etc.

(iv) Cost Audit by Trade Association:

The trade association may like to go for cost audit to ascertain the truth and fairness of costing information provided by the member units.

(v) Cost Audit by Lenders / Institutions:

Lenders / Financing institutions may order cost audit where the assisted unit is suspected to be making losses on continuous basis by selling goods below cost with / without knowing so.

(vi) Statutory Cost Audit:

Statutory Cost Audit is conducted as per the provisions of Section 233B of the Companies Act.

What Constitutes Cost Accounting Records:

Reproduced below are the guidelines pronounced by Cost and Management Accountants in Practice (CAMAP), Bombay regarding the books of accounts required to be maintained to comply with the requirements of the cost accounting record rules:

"The records contemplated under section 209(1)(d) of the Companies Act, 1956 would include all the accounting records maintained by the Company and made available for audit by the financial auditor. In addition, the following records would also have to be maintained:

1. Production
    - 1.1 Raw material consumption register/report;
    - 1.2 Production report;
    - 1.3 Rejections/wastages/scrap report;
    - 1.4 Report on stoppage of machines with reasons;
    - 1.5 Idle time report with reasons;
    - 1.6 Machine utilisation report.

2. Work-in-progress and finished goods
    - 2.1 Process stock register-cost centre wise and product-wise
    - 2.2 Finished goods stock register-product-wise

3. Repairs and maintenance
   3.1 Works order register/card showing materials and spares consumed and labour utilised;
   3.2 In case of workshop, additional records as described under 1(1) above

4. Utilities (steam, power, water)
   4.1 Record of inputs and outputs;
   4.2 Record of cost centre-wise allocation of outputs

5. Raw materials and stores
   5.1 Goods received register;
   5.2 Bin cards;
   5.3 Materials / stores ledgers.

6. Wages and salaries
   6.1 Attendance registers / sheets;
   6.2 Wages / salary sheets;
   6.3 Leave and gratuity payments.

7. Overheads
   - Details as production hours, labour hours, and machine hours to facilitate distribution to production.

8. Cost Accounts
   8.1 Overheads analysis register;
   8.2 Cost centre-wise assets register;
   8.3 Product ledger;
   8.4 Annexures and proforma as per the rules;

9. Sales: Sales Analysis by products.

Verification of Stores:

1. Detailed and adequate records to show the receipts, issues and balances both in quantity and value of consumable stores should be maintained;

2. The value shall include all indirect charges upto works;
3. The valuation of the issues and balances need not be done on a perpetual basis but can be done at periodic intervals, the interval, however, not to exceed one month;
4. Control accounts could be maintained for groups of stores items and such accounts should be reconciled with individual accounts at least once a year;
5. Issues of stores to various heads should be charged to such heads accordingly;
6. Issues of stores for capital works should be so charged and capitalised;
7. The valuation method adopted should be reasonable and shall be applied consistently;
8. The method of valuation should be indicated in the costing records;
9. Any loss of these items either transit, storage or otherwise should be shown separately;
10. The method of treating such losses in determining the cost of the product shall be indicated in the costing records.

Distinction between Cost Audit and Financial Audit:

S. No.	Financial Audit	Cost Audit
1.	The financial audit is compulsory for all companies under Companies Act, 1956.	The cost audit is not compulsory for all the companies.
2.	The object of a financial audit is to see that the books of accounts have been properly maintained	The object of a cost audit is to see that the expenses have been incurred properly and wisely in the best interest of the company
3.	Financial audit certifies that the profit and loss account shows a true and fair view of the affairs of the company.	Cost audit certifies that unit cost of production has been properly determined.

4.	The scope of a financial audit is a bit limited	The scope of a cost audit is wider as it is carried on with broader objectives
5.	There is no need for seeking the prior approval of the Central Government regarding the appointment of a financial auditor.	In case of a cost auditor, the previous approval of the Central Government is necessary.

Distinction between Cost Audit and Management Audit:

S. No.	Cost Audit	Management Audit
1.	Cost audit is the verification of cost records to measure the internal efficiency of the concern	Management audit investigates and develops the relationships with the outside world and internal efficiency of the concern.
2	Under the cost audit, a continuous audit programme is fixed for one year.	Management audit covers a very wide area and it will involve an appraisal of long term policies and plans.
3.	In case of a cost audit the cost auditor checks the cost accounting records with a view that these represent a true and fair view.	In the case of a management audit, the management auditor investigates the aims and objects of the concern.
4.	The government regulations have made cost audit compulsory or obligatory by amending Section 209 of the Companies Act, 1956.	Management audit is not prescribed by the law.

5.	A cost auditor is supposed to submit his cost audit report to Central Government within 120 days.	A management auditor is required to submit his report to the company and no time limit is fixed for the submission of such a report.

Cost Audit (Report) Rules, 2001:

Under Section 233B(4) of the Act, the Cost Auditor appointed by a Company is required to make report to the Central Government in the form, and within such time as may be prescribed by the Central Government, and at the same time forward a copy of the report to the Company. This report should be in accordance with the Cost Audit (Report) Rules, 2001 .

* * *

Review Questions

1. What is meant by Cost Audit? State its objectives.
2. Explain the nature and scope of Cost Audit.
3. State the points to be considered before taking up Cost Audit.
4. How will you conduct Cost Audit?
5. Distinguish between Management Audit and Cost Audit.
6. Explain the qualifications of a Cost Auditor. How is a Cost Auditor appointed?
7. Explain the powers and duties of a Cost Auditor.
8. What a note on Cost Audit programme.
9. Enumerate the liabilities of a Cost Auditor.
10. Differentiate Cost Audit from Financial Audit.
11. Highlight the special features of Cost Audit (Report) Rules, 2001.
12. What are the specific objectives of cost audit on behalf of the management.

[C.S. June2000]

13. Management requires information about each and every functional area of management. In the following functional areas, what aspects would be covered in the management information system (MIS) :

a. plant and equipment
b. personnel
c. production
d. stocks and
e. purchasing.

[C.S. Dec. 2000]

14. Write a review of internal control system in respect of purchasing operation.

[C.S. Dec. 1998]

15. As a cost auditor, describe the procedure you would adopt with regard to labour and material costs.

[C.S. June 1998]

16. State the scope, functions and advantages of the cost audit. Mention the different types of cost audit.

[C.S. Dec. 1997]

17. Explain the salient features of the cost audit (Report) Rules 1968.

[C.S. Dec. 1996]

18. As a cost auditor; describe the procedure you would adopt with regard to:

a. Materials
b. Overheads and
c. Labour [C.S. June 1996]

LESSON 8

REGISTERS AND RETURNS

Objective:

After reading this lesson, the students should be able to under stand the meaning of Statutory and Other Books of a Company; Statutory Books; Non-Statutory or Optional Books; Various Returns, Returns to be filed with Registrar of Companies ;

Learning Activities:

Reading of

i. Filing of forms and Returns and Application under Company Law
by K.V.Shanbhogue,
Law Publishing House, Ahemadabad.

ii. Company Law Procedures by M.C.Bhandari,
Wadhwa Publishers, Nagpur.

iii. Company Secretarial Practice
by P.K.Ghosh & Dr.V.Balachandran
Sultan Chand & Sons, New Delhi.

iv. Company Notices, Meetings & Resolutions
by A.M.Chakraborthi by Taxmann Publications

v. ICSI Study Materials

- Statutory and Other Books of a Company:
- Statutory Books:
- Non-Statutory or Optional Books:
- Statutory Books:
- Register and Index of Members:
- Register and Index of Debenture holders:
- Foreign Registers of Members and Debenture holders:
- Minute Books:

- Register of Charges:
- Register of Directors, Manager, etc.:
- Register of Director's Holding in Shares and Debentures:
- Register of Contracts in which Directors are Interested:
- Register of Fixed Deposits:
- Register of Loans & Investments:
- Non-Statutory Books:
- Application and Allotment Book:
- Register of share warrants:
- Register of Transfers:
- Register of Certified Transfers:
- Register of Documents Sealed:
- Dividend Mandates Register:
- Returns to be filled with Registrar:
- Annual Return:
- Balance Sheet and Annual Accounts:
- Return as to Allotment:
- Return as to Increase of Nominal Share Capital:
- Return of Director, etc.:
- Return of Charges:
- Return of Foreign Companies:
- Companies to file Documents with the Registrar of Companies in Computerised Format:

Statutory and Other Books of a Company:

Every limited company is required to maintain different books and registers for the purpose of record as well as to secure efficiency in operation. Some of these books have to be maintained compulsorily by all companies under the provisions of the Companies Act. These are known as Statutory Books. There are some other books which are not required to be kept under the law, but which most companies maintain for the proper an deficient running of the company. These are known as non-Statutory or Optional Books. Failure to comply with the provisions of the Companies Act relating to the maintenance of Statutory Books will make the directors, secretary and other officers of the

company liable to penalties. It is the duty of the secretary, as the principal executive officer, to supervise the proper maintenance of these books.

Statutory Books:

1. Register and Index of Members [Sec.150 and 151]
2. Register and Index of debenture holders [Sec.152 and 154]
3. Foreign Registers of Members and debenture holders [Sec.158]
4. Register of Mortgages and Charges [Sec.143]
5. Register of Investments not held in company's name [Sec.49]
6. Minute Books [Sec.193 and 194]
7. Register of Directors, Manager, etc. [Sec.303]
8. Register of Directors' holding in Shares and Debentures [Sec.307]
9. Register of Contracts in which Directors are interested [Sec.301]
10. Books of Accounts and Annual Accounts [Sec.209 and 210]
11. The Annual Return [Sec.159 to 161].
12. Register of Loans & Investments [Sec.372A]
13. Register of Fixed Deposits [Sec.58A]
14. Register of Renewed and Duplicate Certificates

Non-Statutory or Optional Books:

In addition to the statutory registers and books which are required to be maintained compulsorily, companies also maintain certain other books and registers for securing efficiency in the operation of the company. These may be called non-statutory or optional books. Although maintenance of these books is not obligatory 'Companies invariably maintain them to help in keeping records of various operational and ministerial work connected with the running of the company's affairs. There are no hard and fast rules as to the number or nature of optional books to be maintained by a company. Each company decides on the number and nature of non-statutory books to be kept according to its particular needs.

A list of non-statutory books usually maintained by a company is given below:

1. Share application and allotment book.
2. Register of transfers or share transfer register.
3. Register of probates, letters of administration etc. in respect of transmission of shares
4. Register of lost share certificates
5. Register of Certification
6. Register of balance tickets
7. Register of share warrants
8. Dividend books or register
9. Dividend mandates register
10. Register of documents sealed
11. Register of powers of attorney and other documents received
12. Directors' attendance book
13. Agenda book
14. Call book

Statutory Books:

Register and Index of Members:

(a) Every company is required to maintain a Register of Members in one or more books [Sec.150].

(b) The register must contain the particulars about members as prescribed in the Act, viz., name, address, occupation, shares or stock held, date of becoming member, date of ceasing to be a member [Sec.150]. The register should be in conformity with the format prescribed under Rule 7 of the Companies (Issue of Share Certificates) Rules, 1960.

(c) The register can be closed with 7 days' prior notice, but it cannot be closed for more than 30 days at a stretch or for more than 45 days in a year. The notice must the given by advertisement in some newspapers circulating in the district in which the registered office of the company is situated [Sec.154(1)]. If the register is

closed without giving prior notice, or closed for a continuous period or an aggregate period exceeding the limits specified, the company and every officer of the company who is in default shall be punishable with fine which may extend to Rs.500 for every day during which the register is so closed [Sec.154(2)].

(d) Every company having more than 50 members is required to maintain an Index of members, unless the register itself is self-indexed. Any alteration made in the Register of Members must be recorded in the Index within 14 days [Sec.151].

Register and Index of Debenture holders:

Every company is required to maintain in one or more books a register of debenture holders. The register is to be maintained only in respect of registered debentures. No such register is necessary for bearer debentures. The register shall contain the following particulars of debenture holders:

(a) name, address and occupation

(b) the debentures held by each holder

(c) the date when the name of each holder was entered in the register, and

(d) the date when he ceased to be a debenture holders. Every company with more than fifty debenture holders must also maintain an index of debenture holders, unless the register is in itself an index. Regarding the restrictions imposed on the closing of the register of debenture holders, the provisions of the Act are the same as in the case of register of members [Sec.152 and 154].

Foreign Registers of Members and Debenture holders:

A company with share capital or which issued debentures may, if so authorised by its Articles, maintain branch registers of members and debenture holders resident in that State or country [Sec.157(1)]. These are called Foreign Registers. However, the company must file a notice with the Registrar informing him of the situation of such a foreign register or any change in the situation or discontinuance of such register within 30 days [Sec.157(2)].

The foreign register of members of debenture holders is deemed to be a part of the principal register maintenance at the registered office of the company in India and all entries made in the foreign register and required to be transmitted to the registered office for incorporation in the principal register. The foreign register is required to be maintained in the same manner as the principal registers maintained at the registered office of the company except that the advertisement before closing the register must be inserted in a newspaper circulating in the district in which the foreign register is kept [Sec. 158].

Minute Books:

Under section 193 of the Companies Act, every company is required to maintain minute books for recording proceedings of every general meeting board meeting and meeting of every committee of the board. The pages of the minute books must be consecutively numbered and each page must be initialed and the last page of the proceedings of each meeting must be dated and signed by the chairman in the minutes book within thirty days of the conclusion of such meeting. The minutes of proceedings of the meeting cannot be attached or pasted to the pages of minute books.

Under section 196, the minutes book containing proceedings of general meeting must be kept open for inspectional t the registered office of the company for at least two hours during business hours every day. A member can also ask for a copy of the minutes at a notice of seven days of payment of such sum as may be prescribed for very one hundred words or fraction thereof. However, the minutes book containing proceedings of Board meetings cannot be inspected by members as it contains confidential information relating to the business and management policies of the company which cannot be divulged to members in general. The directors have full right to inspect the minutes book of Board Meetings.

Register of Charges:

(a) Every company is required to maintain a register of charges and mortgages at its register office [Sec.143(1)].

(b) Particulars of all charges and mortgages specifically affecting property of the company and all floating charges on the undertaking or any property must be entered therein. In each case, the following particulars are to be recorded:

a. A short description of the property charged;

b. The amount of the charge; and

c. Except in the case of securities to bearer, the names of the persons entitled to the charge [Sec.143(1)].

(c) The register must be kept open for inspection at the register office for at least two hours every working day, by creditors and members free of charge, and by any other person on payment of a fee of such sum as may be prescribed of. (Substituted for 'one rupee' by the companies (Amendment) Act, 1988).

Register of Directors, Manager, etc.:

Every company must keep at its registered office a register of its directors, managing director, manager and secretary. The register should contain all particulars with respect to each of the officers, viz., his name and surname, residential address, nationality, business, occupation, particulars of the office held, date of birth, etc. The names and particulars of companies nominating directors have also to be included in the register. The company must send to the Registrar of Companies a return in duplicate as per form prescribed giving the particulars contained in the register within 30 days from the date of appointment of the first director. Similarly, changes among the managerial personnel and any change in the particulars of the register are to be notified to the Registrar within 30 days from the date of such change (sec. 303).

Register of Director's Holding in Shares and Debentures: .

Under the company has to maintain a register of particulars about the shares and debentures held by directors in the company, its holding company or its subsidiary company, which are held by him or in trust for him, or of which he has any right to become a holder wither on payment or not. Specifically, it is required that the nature and extent of any payment or not. Specially, it's required that the nature and extent of any payment or not. Specially, it is

required that the nature and extent of any interest or right in or over any shares or debentures recorded in relation to a director in the same register shall if he so requires, be indicated in the register. For purposes of this record, anybody in accordance with whose direction the Board of a company is accustomed to act is to be treated as direct. Further, a director will be deemed to hold or to have interest in or right over the shares and debentures of a company if any other company holds them or has interest or rights in or over them, and either the company or its Board of Directors is accustomed to act in accordance with his directions or instructions; or he is entitled to exercise or control the exercise of one-third or more of the total voting power exercisable at any general meeting of that company. Every director of a company must give notice in writing of purchase or sale of shares to the company, so that the register can be kept up to-date.

Register of Contracts in which Directors are Interested:

Sec. 301 of the Companies Act requires that the following particulars regarding contracts with other concerns in which directors of a company are interested should be recorded in a separate register:

(a) the date of the contracts;

(b) the name of the parties to such contacts or arrangements;

(c) the principal terms and conditions thereof;

(d) the date when a contract of this type was placed before the Boar of Directors; and

(e) The names of directors voting for and against the contract and of those remaining neutral [Sec.301(1)].

The register must also specify, in relation to each director the names of the firms and companies, of which notice has been given by him under Section.299(3) [Sec.301(3)].

Register of Fixed Deposits:

Section 58A o the Companies Act allows all types of non-banking and non-financial companies to accept deposits from the public or its members, subject of the limit, manner and conditions prescribed by the Central

Government in this behalf. Accordingly the framed the companies frames the Companies (Acceptance of Deposits) Rules, 1975, which prescribe the limits, manner of accepting public deposits and other relevant rules in this respect.

Under Rule 7 of the Acceptance of Deposit Rules every company accepting deposits from the public must maintain a Register or Registers where particulars of the deposit from each depositor must be entered. The following particulars are required to be entered in the register separately for each deposit:

(a) name and address of the depositor;

(b) date and amount of deposit;

(c) duration of the deposit and the date when the deposit will be repayable;

(d) rate of interest;

(e) date or dates on which payment of interest will be made;

(f) any other particulars relating to the deposit.

The Register or Registers of deposits must be preserved in good order for a period of not less than 8 years from financial year in which the last entry is made.

Register of Loans & Investments:

Section 372A of the Companies Act provides that no company can make any loans or give any guarantee or provide any security in connection with any loans to other companies under the same management, unless it is previously authorised by a special resolution of the lending company.

Every such lending company must keep a register in which the following particulars must be entered:

(a) the names of all bodies corporate under the same management as the lending company, and the name of every firm in which partner is a body corporate under the same management as the lending company; and

(b) the following particulars in respect of every loan made, guarantee given or security provided by the lending company in relation to any such body corporate under this section:

(i) the name of the body corporate to which the loan has been made before or after that body corporate came under the same management as the lending company;

(ii) the amount of loan;

(iii) the date on which the loan has been made.

Every investing company must keep a register of all investments made by it in shares of other companies, showing in respect of each investment the following particulars;

(a) the name of the body corporate in which the investment has been made;

(b) the date on which the investment has been made;

(c) where the body corporate is in the same group as the investing company the date on which the body corporate is in the same group;

(d) The names of all bodies corporate in the same group as the investing company.

Non-Statutory Books:

Application and Allotment Book:

After the last date for receipt of applications for shares is over and the applications are collected from the bankers, particulars of the applications are entered in the Application and Allotment List or Book. When allotment of shares is made by the Board these are entered in the appropriate columns of shares is made by the Board these are entered in the appropriate columns of the book. This book is maintained to facilitate work of allotment.

Register of Share Warrants:

Under the provisions of companies act, the name of the member to whom a share warrant has been issued is struck off the Register of Members. On the issue of the share warrants, the names and other particulars of these members are entered in a separate register known as Register of Share warrants. The register contains particulars of the warrants issued and warrants surrendered. When any member surrenders his share warrant and applies for re-entry of his name in the Register of Members, the particulars of such surrender are entered and his name struck off the Register of Share Warrants.

Register of Transfers:

The maintenance of the register is not compulsory under the law, but most companies maintain such a register. After the transfer deeds have been received, transfer receipts have been issued and notice of lodgment of transfer is issued, the secretary waits for objections from the transferor or transferee, if any. If no objection is received, he enters the details of the transfer in the Register of Transfers. The particulars entered therein are: number of transfer, date of registration, date of Board meeting approving the transfer, name and address of transferor, the number of shares transferred with distinctive numbers, the name, address and description of the transferee, number of new certificate issued, etc. The register is placed before the Board meeting t the time of approval of the transfers along with other documents.

Register of Certified Transfers:

This register is maintained to record the particulars of certified transfers, viz., number and date of the certificate, number of certificate to be cancelled, transfer certificate number date of registration of transform names of transferor and transferee etc. the particulars are entered in the register after the secretary gets back the certified instrument of transfer from the transferee for registration. The register is placed before the Board meeting for approval of the transfer along with the certified instrument, cancelled share certificate, and the net share certificate.

Register of Documents Sealed:

Though not compulsory under the law, all companies maintain a register of documents sealed. Since the seal is the signature of the company, every care should be taken to keep the seal in safe custody and to maintain an accurate record of the documents sealed to prevent improper use of the seal. Whenever a document is sealed the necessary particulars (viz., number and date of the resolution authoring the sue of seal the date of scaling, particulars of documents sealed persons in whose presence the seal is affixed, location of document, etc.), are entered in the register.

Dividend Mandates Register:

A 'Mandate' is a letter of request or instruction. Normally many of the shareholders of a company request the company to pay the dividend payable to them directly to their bankers. This is done by sending a Dividend Mandate' in the prescribed form to the company. On receipt of these mandates, the secretary scrutinizes them and enters the particulars of these mandates in the Dividend Mandates Register, so that the mandates can be complied with a t the time of payment of dividends.

Returns to be filled with Registrar:

Under the provisions of the Companies Act, 1956, a company has to file various returns and statements with the Registrar of Companies. These returns are of two kinds:

(b) Periodical Returns, and
(c) Casual Returns.

Periodical returns are those which have to be filed with the Registrar regularly at periodical intervals such as once in a year or half-year. The two most important periodical returns are:

(a) the Annual Return under section 159; and
(b) the Balance Sheet and Profit and Loss Account under Sec. 220.

Casual returns are those which have to be filed with the Registrar as and when necessary or on the occurrence of certain transactions in the ordinary course of the company's business. Some important types of causal returns are:

(a) Return as to alternation of memorandum [Sec.18];
(b) Return as to allotment [Sec. 75];
(c) Return as to issue of bonus shares [Sec.75].
(d) Return of increase of share capital [Sec. 94-A].
(e) Return of charges [Sec.125].
(f) Return of beneficial ownership in shares [Sec.1787-C].
(g) Return of directors [Sec.303].
(h) Return of appoint of managing / whole time director [Sec.314];
(i) Return of final meeting(s) in members' / creditors' voluntary winding up [Sec.497 & 509].
(j) Return by foreign companies [Sec. 592 & 593].

Annual Return:

Every company having a share capital must file an Annual return with the Registrar. The Annual Return must be filed very year within 60 days of the annual general meeting (sec. 159). The original of the return is maintained at the registered office of the company as part of the Register of Members.

The annual return of every company must be prepared in the form prescribed in Part II of Schedule V of the Act or as near thereto as possible.

The annual return must be kept at the registered office of the company or any other place within the same city provided that other palace has been approved by a special resolution of the general meeting and an advance copy of the resolution has been filed with the registrar. The annual return must be open to inspection of members. debenture holders and other persons and copies of the returns may be taken by members, etc. in the same manner as in the case of register of members (Sec.163).

Balance Sheet and Annual Accounts:

Under the provisions of section 210 of the Companies Act, 1956, at every annual general meeting held as per the provisions of section 166, the Board of directors of a company has to lay before the company a Balance Sheet as at the need of the preceding financial year and a Profit and Loss Account for the relevant financial year. Under section 211, the balance sheet and profit and loss account shall be in the form set out in parts I and II of schedule VI to the Act, or as near thereto as circumstances admit.

Section 220 of the Companies Act provides that three copies of the Balance Sheet and Profit and Loss Account of the company, along with the Auditors' Report, Directors' report and other documents required to be annexed thereto, must be filed with the Registrar of Companies within 30 days of the annual general meeting, or if the AGM is not held, within 30 dads from the latest day on or before which the AGM ought to have been held.

Return as to Allotment:

Section 75 of the Companies Act provides that, whenever a company having a share capital makes any allotment of shares, it must, within 30 days hereafter, file with the Registrar a return of allotment starting therein –

(a) the number and nominal amount of the shares comprised in the allotment;
(b) the names, address and occupations of the allottees; and
(c) the mount, if any, paid or due and payable on each share.

The company shall not show in such return any shares as having been allotted for cash, if cash has not actually been received. In the case of shares allotted for consideration other than cash, the return must state the number and nominal amount of shares so allotted, the extent to which they are to be treated as paid-up, and the consideration for which they have been allotted.

In case of bonus shares, the company must file with the Registrar a return stating the number and nominal amount of such shares comprised in the allotment and the names, addresses, occupations of the allottees. Along with the return a copy of the resolution authorizing the issue of bonus shares must also be filed.

Return as to Increase of Nominal Share Capital:

Section 94-A of the Companies Act provides that, where the central government, by order made under Section 81(4), directs that any debentures issued to, or loans raised form the Government by a company shall be converted into shares in the company, the order will have the effect of automatically altering the capital clause of the Memorandum of the company by increasing the nominal share capital [sub-section (1)].

Return of Director, etc.:

Under the provisions of section 303 of the companies act, every company is required to kept at its registered office a register of its directors, managing director, manager and secretary, containing the particulars specified in sub section (1).

Section 303 also provides that the company must send to the Registrar a return in duplicate in the prescribed form, containing the particulars specified in the said register, and notification in duplicate in the prescribed form of any change among its directors, managing director, manager or secretary, specifying the date of change. The return is to be filed in Form No.32 within 30 days from the date of the appointment of the first directors of the company and within 30 days from the date of the happening of any change [sub-section (2)].

Return of Charges:

Section 125 of the Company Act provides that, every charge created by a company, being a charge to which this section applies, shall be avoid as against the liquidator and any creditor of the company, unless the prescribed particulars of the charge, together with the instrument by which the charge is created, or a copy thereof, are filed with the Registrar for registration within 30 days after the date of the creation of the charge.

Return of Foreign Companies:

1. Under section 592 of the Companies Act, foreign companies having a place of business in India are required to deliver to the Registrar for registration, within 30 days of the establishment of the place f business, the documents and particulars specified in clauses (a) to (e) of sub-section (1). The

information required under Section 592 is to be filed in Form No.44 Central Government General Rules and Forms, 1956

2. Section 593 of the Act provides that, if any alteration occurs or is made by a foreign company in nay of its documents (charter, statutes, or memorandum and articles), its directors or secretary, or in the principal place of business in India, the company must deliver to the Registrar for registration a return containing the prescribed particulars of the alternation, within the prescribed time.

Companies to file Documents with the Registrar of Companies in Computerised Format:

A new Sec.610 A has been inserted by the Companies (Amendment) Act, 1996, which provides the facility to a company to file its returns in computerised format. According to Sec.610-A(1) of the Companies Act, 1956, information contained in a micro film of a document or the reproduction of the image, a facsimile copy of a document, computer print outs and documents on computer media shall be deemed to be also a document for the purpose of this Act. They shall be admissible in any proceedings, without further proof on production of the original as evidence of any contents of the original. However, at the ROC office, necessary checks would be carried out while receiving returns or documents on computer media. The Registrar would take due care to preserve the computer media by duplicating, transferring, mastering or storage without loss of data.

Important Returns to be Filed with Registrar of Companies

Section	Description of Document, Return, notice, etc. to be filed, time within which to be filed and prescribed from etc.
1	2
18(1) & 3	Certified copy of order of CLB confirming alteration of memorandum – within three months
23(1)	Special resolution u/s.21 regarding change of name of company – within 30 days – in Form No.21

33(1) & (2)	Memorandum / Articles / Proposed agreement, if any, for appointment of managing / whole-time director or manager and Declaration of compliance u/s33(1) – before registration of company – in Form No.1
60(1)	Copy of Prospectus – on or before date of publication of prospectus – in Form prescribed in Schedule II to the Act.
75(1)	Return of allotment – within 30 days from date of allotment or extented time allowed by Registrar – in Form 2
75(2)	Particulars of contract relating to shares allotted otherwise than in cash where the contract is not reduced to writing – within 30 days after allotment - in Form 3.
125(1)/134	Particulars of charges created together with instrument, if any, creating / evidencing charge – with instrument, if any, creating / evidencing charge – within 30 days of creation of charge – Form 8
141	Order of Company Law Board extending time of filing particulars / registration of charge of modification or register of charges – Form 21
149(2A)	Declaration of compliance with Sec.149(2A)(i) or (2B) with respect to commencement of new business – before commencement – Form 20A
269(2)	Return of appointment of managing / Whole-time Director or manager in accordance with Sch.XIII concerned – within 90 days of appointment – prescribed form.

* * *

Review Questions

1. What registers of a company can be inspected by its members?
2. Write short notes on the following:
   i. Register of Contracts, Companies and rims in which directs are interested
   ii. Register of renewed and duplicate share certificates
   iii. Register of Members and Annual Return
3. Who is entitled to inspect or to have the copy of the following :
   i. Register of members
   ii. Register of contracts
   iii. Register of charges
   iv. Minutes of Board meetings
4. What information must be entered in the Register of charges maintained by the company? What is the effect of failure to register a registerable charge?
5. What are the provisions of the Companies Act, 1956 with regard to inspection of register of directors etc.
6. State the provisions of the Companies Act, 1956 relating to annual return

MODEL QUESTION PAPER

Paper 2.2: SECRETARIAL AND MANAGEMENT AUDIT

Time : 3 hours Maximum Marks: 100

PART – A (5 x 8 = 40 marks)

Answer any **Five** questions

1. Define a company secretary in practice. Who are eligible to practise?
2. What is meant by Secretarial Audit? State the appointment and qualifications for Secretarial Auditors?
3. What is meant by Search & Status Report? Explain the objectives of preparing such reports.
4. What is meant by Securities Audit? What are its objectives?
5. Explain the need for and scope of Secretarial Compliance Report.
6. Explain the features and objectives of Management Audit.
7. What are the objectives and types of Cost Audit?
8. State the provisions of Companies Act relating to Annual Return.

PART – B (4 x 15 = 60 marks)

Answer any **Four** questions

9. Discus the Various areas of practice exclusively given by the statute to the practicing company secretaries.
10. You are appointed as Secretarial Auditor of X Ltd. How would you commences the Audit and which of the data and records would you examine.
11. Enumerate the important points to be considered while preparing a search and status report. State the documents to be prepared in connection with search reports.
12. How Securities Audit can be a powerful tool for Investors Protection
13. Prepare a checklist for Secretarial Compliance with regard to
    a) General Meeting
    b) Declaration of Dividend
14. What is meant by Management Audit? Differentiate Management Audit from Financial Audit
15. Discuss the various Registers to be maintained by a company statutorily.

* * *

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